Contents

Volume 1

Preface
Acknowledgments
About the Authors of the Fourth Edition
About the 2009 Update Authors
Selected Developments
Cutoff Dates and CEB Citation

1 Lawyer's Role in Real Property Sales

2 Brokers
Randall I. Barkan
Jeffrey H. Belote

3 Letters of Intent
Jamie O. Harris
Steve Stwora-Hail

4 The Purchase and Sale Agreement
Jennifer R. Bae
Timothy N. Brown
Sherry L. Geyer

5 Specialty Commercial Purchase and Sale Agreement Provisions: Hotels
Timothy N. Brown

6 Residential Purchase and Sale Transactions
Howard L. Pearlman

7 Hazardous Waste Considerations
Kenneth S. Kramer
William D. Wick

Volume 2

8 Options, Rights of First Refusal, Puts, and Similar Rights
Nolan M. Kennedy
Thomas H. Jamison
Gordon K. Eng

9 Seller Financing
Alice L. Akawie
Lauren M. LaPietra

W. Stephen Wilson

10 Deeds
Scott A. Sommer

11 Descriptions of Property
Scott A. Sommer

12 Covenants of Title
Scott A. Sommer

13 Property Insurance
Timothy R. Sullivan

14 Liability Insurance: Selected Issues Pertinent to Sales
Timothy R. Sullivan

15 Escrow and Closing the Sale
Peter Brian Bothel
Laura S. Lowe

Appendixes

Appendix A—Transfers Triggering Reappraisal

Appendix B—Buyer's Comprehensive Commercial Property Acquisition and Due Diligence Checklist

Appendix C—Checklist of Due Diligence Materials to Be Delivered by Seller to Buyer in Sale Involving Commercial Leases

Appendix D—Board Resolution (Authorizing Purchase)

Appendix E—Limited Liability Company Certificate (Authorizing Purchase)

Appendix F—Statement of Partnership Authority (Secretary of State Form GP-1)

Appendix G—Grant Deed

Appendix H—Bill of Sale

Appendix I—Assignment of Leases

Appendix J—Assignment of Intangibles

Appendix K—Estoppel Certificate From Tenants

Appendix L—Tenant Letter

Appendix M—Spousal Waiver

Appendix N—Alternate Natural Hazard Conditions Disclosure

Appendix O—Sample Tenancy-in-Common Agreement

Appendix P—Access License and Indemnity Agreement

Appendix Q—Hotel Purchase and Sale Agreement

Appendix R—Estoppel Certificate From Hotel Operator

Appendix S—Escrow Instructions—General Provisions

Appendix T—Real Estate Withholding—Computation of Estimated Gain or Loss (FTB Form 593-E)

Appendix U—Real Estate Withholding Certificate (FTB Form 593-C)

Appendix V—Real Estate Withholding Installment Sale Agreement (FTB Form 593-I)

Appendix W—FIRPTA Certification

Appendix X—Buyers/Borrowers Estimated Closing Statement

Appendix Y—Settlement Statement

Appendix Z—Supplemental Escrow Instructions—Funds Held

Appendix AA—Escrow Cancellation Instructions

Appendix BB—Preliminary Change of Ownership Report
Directory
Table of Statutes, Regulations, and Rules
Table of Cases
Table of References
Table of Forms
Index

© The Regents of the University of California

Preface

It is hard to imagine a more fundamental area of real property practice than sales transactions. This fourth edition of California Real Property Sales Transactions, like its predecessors, is a practical guide to the myriad issues facing attorneys for both buyers and sellers of commercial and residential real property. These issues range from basic considerations about how title should be held to complex analysis of hazardous substances liability.

The first edition of this book covered a broad spectrum of topics that have since given rise to their own books, including California Title Insurance Practice (2d ed Cal CEB 1997), Real Property Exchanges (3d ed Cal CEB 2002), California Real Estate Finance Practice: Strategies and Forms (Cal CEB 2000), and California Real Property Remedies and Damages (2d ed Cal CEB 2002).

Subsequent editions added in-depth discussion of special topics such as hazardous wastes and toxic contamination of real property (see chap 7), which are of immense concern to buyers and sellers of real property; disclosure requirements imposed on both brokers and sellers of real property (see chaps 2, 6); basic property insurance principles, types of policies offered, and risk-of-loss issues (see chap 13); and the advantages and disadvantages of using letters of intent (see chap 3).

This fourth edition continues this expansion into more sophisticated practice areas by including two new chapters and three new forms:

- Chapter 5 discusses and analyzes the specialty commercial provisions unique to the purchase and sale of hotel properties. Three new appendixes provide a complete attorney-drafted hotel purchase and sale agreement (see App Q); a hotel operator estoppel certificate (see App R); and an access license and indemnity agreement that allows a prospective buyer to enter the property to perform its due diligence (including conducting inspections and testing) (see App P);
- Chapter 14 examines liability insurance issues pertinent to purchase and sale transactions.

In addition, the chapter on brokers (see chap 2) was thoroughly reorganized and rewritten to focus more closely on ethical and liability issues such as dual agency, disclosure obligations, the broker's role in negotiating contracts, and how brokers may avoid the unlicensed practice of law in handling real property sales. The chapter on residential purchase and sale transactions (see chap 6) was also extensively rewritten. The options chapter (see chap 8) was expanded to cover rights of first refusal, puts, and similar rights. Thoroughly updated and revised, this fourth edition provides the real estate lawyer with even more detailed and comprehensive coverage of all aspects of a purchase and sale transaction.

We are fortunate to have as authors of this book the real property practitioners listed on the Contents page and the first page of each chapter. To all these authors, who generously gave their time in writing their chapters, we express our profound gratitude. In addition, CEB acknowledges two attorneys whose contributions to this book have been invaluable. For many years, C. Darrell Sooy of Tobin & Tobin, San Francisco, acted as the update author, providing essential insight into developments in the law affecting real property sales transactions. Stephen K. Cassidy of Cassidy, Shimko, Dawson & Kawakami, San Francisco, acted as "super consultant" for this fourth edition by reviewing the third edition of this book and providing constructive comments and suggestions for improvement.

We are also indebted to the attorneys who served as authors of previous editions, update authors, and consultants on this book. Their names are listed on the Acknowledgments page.

CEB plans to update this book on a regular basis. We solicit your suggestions and comments to help us keep it accurate and up to date.

CEB Attorney Editors Janis L. Blanchette (Managing Editor), Ann H. Davis, and Bonnie C. Maly, and Legal Editors Ragnhild Fougner, Marty Weis, Philip Weverka, Kenneth Marr, and Carolyn Valley contributed to this fourth edition. Administrative support was provided by Nila Kanzaria and Akanke Peyton. Paul Green handled copy editing and production. Kathryn Te Selle and Robert Burke updated the index. Composition was performed by CEB's Electronic Publishing staff.

December 2009 Update

CEB wishes to thank the authors of this update, Randall I. Barkan, president of Realdispute Consulting & Expert Witness Services, Pacific Grove; Jeffrey H. Belote, partner with the firm of Carroll, Burdick & McDonough LLP, San Francisco; Peter Brian Bothel, senior associate with the firm of Cassidy, Shimko, Dawson & Kawakami, San Francisco; Gordon K. Eng, shareholder with the firm of Brown Winfield Canzoneri Abram Inc., Los Angeles; Theani C. Louskos, principal with the firm of Bartko, Zankel, Tarrant & Miller, San Francisco; Laura S. Lowe, counsel with Miller, Starr, Regalia, Walnut Creek; Steven M. Muldowney, partner with Cox, Castle & Nicholson LLP, Orange County; Peter S. Muñoz, partner with Reed Smith, LLP, San Francisco; Howard L. Pearlman, principal with Bartko, Zankel, Tarrant & Miller, San Francisco; Scott A. Sommer, partner at Pillsbury Winthrop Shaw Pittman, LLP, San Francisco; Arthur O. Spaulding, Jr., managing partner of the Irvine office of Cox, Castle & Nicholson LLP; Steve Stwora-Hail, partner with Downey Brand LLP, Sacramento; Timothy R. Sullivan, of counsel with McCormick, Barstow, Sheppard, Wayte & Carruth LLP, Fresno; William D. Wick, partner with Wactor & Wick LLP, Oakland; and Sara Hansen Wilson, partner with Drinker Biddle & Reath, LLP, San Francisco.

CEB Attorney Editor Janis L. Blanchette and Legal Editors Mary Claugus, Philip Weverka, and Kenneth Marr contributed to this title. Administrative support was provided by Kenya Denman and Nila Kanzaria. Dorie Riepe handled copyediting and production. Kathryn Te Selle updated the index. Composition was performed by CEB's Electronic Publishing staff.

John K. Chapin
Practice Group Manager
Real Property

Pamela J. Jester
Director

© The Regents of the University of California

Acknowledgments

The following attorneys have contributed greatly to the material in this book. Some served as authors for one of the first three editions. Subsequent authors benefited from their work and incorporated it into the current edition. Others either served as consultants on one or more editions of this book, by reviewing and commenting on one or more chapter manuscripts, or acted as update authors since publication of the third edition. Their valuable suggestions have made the book more accurate and more reflective of practice throughout the state. To each of them, our special thanks.

Alice L. Akawie
Akawie & LaPietra, Oakland
Russell J. Austin
Marron, Reid & Sheehy, Sacramento
Jennifer R. Bae
Sun Microsystems, Inc., Santa Clara
David W. Bagley II
Hecht, Solberg, Robinson & Goldberg, LLP, San Diego
Lynn A. Bersch
Crosby, Heafey, Roach & May, San Francisco
Lynne H. Blair
Valencia
Timothy N. Brown
Crosby, Heafey, Roach & May, San Francisco
Richard A. Bruzzone
Crosby, Heafey, Roach & May, Oakland
Joan Cambray
Wendel, Rosen, Black & Dean LLP, Oakland
Stephen K. Cassidy
Cassidy, Shimko, Dawson & Kawakami, San Francisco
Natasha C. Chalmers
Crosby, Heafey, Roach & May, San Francisco
Eun-Hee Chang
Crosby, Heafey, Roach & May, Oakland
Llewellyn P. Chin
California Association of REALTORS®, Los Angeles
Philip H. Ebling
Heller Ehrman White & McAuliffe LLP, San Francisco
James R. Eskilson
Crosby, Heafey, Roach & May, Los Angeles
Robert T. Flick
Katten Muchin & Zavis, Los Angeles
Sherry L. Geyer
First Republic Bank, San Francisco
John E. Gutierrez
Berkeley
Mark Hagarty
Luce, Forward, Hamilton & Scripps, LLP, San Diego
James L. Hillman

Oakland
Eric D. Horodas
Rubinstein & Perry, LLP, San Francisco
Philip L. Jelsma
Luce, Forward, Hamilton & Scripps, LLP, San Diego
Michael J. Kaminsky
Crosby, Heafey, Roach & May, Los Angeles
Michael S. Klein
Klein & Weisz, Los Angeles
Lauren M. LaPietra
Akawie & LaPietra, Oakland
Joan L. Lesser
Irell & Manella, Los Angeles
Frederick Martin, Jr.
Christison & Martin, San Diego
Nola M. McGuire
Irvine
Paul R. Mohun
Reed Smith LLP, San Francisco
Peter S. Muñoz
Crosby, Heafey, Roach & May, San Francisco
Janet C. Norris
Steefel, Levitt & Weiss, San Francisco
Janice A. Ramsay
Ramsay, Johnson & Klunder, Irvine
Sean R. Rhatigan
Crosby, Heafey, Roach & May, San Francisco
Gary S. Rose
Flynn and Rose, Los Gatos
James D. Schwefel, Jr.
Noland, Hamerly, Etienne & Hoss, Salinas
Alice A. Seebach
Seebach & Seebach, Los Angeles
Shannon Marie Silverman
Linda Hart Chandler, Newport Beach
C. Darrell Sooy
Tobin & Tobin, San Francisco
John F. Soukup
Soukup & Schiff, LLP, Los Angeles
Carolyn Johnson Stein
Wendel, Rosen, Black & Dean, LLP, Oakland
Anthony Theophilos
Starr Finley LLP, San Francisco
John M. Turner
Turner & Williams, Inc., San Diego
Scott C. Verges
Mandel, Budel & Verges, San Francisco
Paul J. Weinberg
Paul J. Weinberg Private Mediation Services, Irvine
Carolyn Weiss
Crosby, Heafey, Roach & May, Los Angeles

James L. Welch
Glenn, Wright, Jacobs & Schell, San Diego
Norma J. Williams
Crosby, Heafey, Roach & May, Los Angeles
W. Stephen Wilson
Tobin & Tobin, San Francisco

© The Regents of the University of California

About the Authors of the Fourth Edition

RANDALL I. BARKAN, coauthor of chapter 2, is the President of Realdispute Consulting & Expert Witness Services in Pacific Grove. Mr. Barkan received his A.B. from Harvard and his J.D. from the University of California, Berkeley, School of Law. After more than 10 years as a business and real estate litigator, he has had a 20-year career as an executive and corporate counsel in the commercial real estate industry (Coldwell Banker Commercial Group, Marcus & Millichap, and TRI Commercial Real Estate Services). He has been a licensed California real estate broker since 1988, and was the designated broker for over 250 sales agents in nine California offices. Mr. Barkan is a former Vice-Chair and Executive Committee member of the State Bar Real Property Law Section, and has been a panelist at numerous State Bar, CEB, and ABA programs on real estate, corporate counsel, and litigation issues.

JEFFREY H. BELOTE, coauthor of chapter 2, has practiced real estate law for 26 years. He is a partner of Carroll, Burdick & McDonough LLP, San Francisco, where he is the Co-Chair of the Real Estate and Construction Litigation Practice Group. He received his J.D. from the University of San Francisco School of Law and his B.A. from the University of Colorado at Boulder. Mr. Belote prosecutes and defends actions in commercial and real estate litigation and has successfully litigated, settled, and when necessary arbitrated and tried multiparty and complex litigation cases. Mr. Belote lectured for several years in Real Estate Law and Real Estate Concepts in the Masters Program at Golden Gate University, and guest lectured in banking law in the Masters Program. Mr. Belote has been a speaker for CEB, the National Business Institute, and California Land Title Association. He is co-author of: "Advanced Real Estate Law in California" (1991), "Easement and Boundary Disputes in California" (1992), "Keys to Success in a Real Estate Transaction in California" (1993). He was an editorial contributor for James Publishing in 1999 for its book entitled "California Causes of Action."

PETER BRIAN BOTHEL, coauthor of chapter 15, has been a senior associate with the firm of Cassidy, Shimko, Dawson & Kawakami, San Francisco, since 2002. His practice emphasizes real property acquisitions and financing, commercial leasing, and other real estate transactions. He was previously a partner in his own firm, where his practice emphasized real estate transactions and litigation, including title, title insurance coverage and escrow, foreclosures, easements, and real estate broker litigation. Mr. Bothel received his J.D. from Duke University School of Law in 1977 and his B.A. from Wheaton College, Illinois, in 1974.

TIMOTHY N. BROWN, author of chapter 5 and the coauthor of chapter 4, recently retired from the San Francisco office of Reed Smith LLP. Mr. Brown practiced in the areas of real estate and environmental law, including the development of office and industrial properties and related land use entitlement matters; the acquisition and disposition of major real estate projects; lease transactions involving a wide variety of office, industrial, and retail properties; real estate finance matters representing lenders, borrowers, and institutional equity investors; and hazardous materials issues in connection with property sales, acquisitions, loans, and leases. Mr. Brown is a member of the American College of Real Estate Lawyers (ACREL), for which he has chaired the Land Use Committee and the Urban Land Institute. Before his retirement he was active in the Real Property, Probate and Trust Law (RPPTL) Section of the American Bar Association, for which he chaired two committees. He has been a frequent speaker at programs sponsored by ACREL, the RPPTL Section, and CEB. He received his A.B. degree from Harvard College in 1964 and his LL.B from Harvard Law School in 1967.

GORDON K. ENG, coauthor of chapter 8, is a shareholder with the firm of Brown Winfield Canzoneri Abram Inc., Los Angeles, where his practice emphasizes real estate acquisition, financing, and development. Mr. Eng has been a member of the Executive Committee of the Real Property Law Section of the State Bar of California and a member of the Financial Institutions Committee of the Business Law Section of the State Bar of California. Mr. Eng has also been a member of the Board of Directors of Habitat for Humanity's Greater Los Angeles affiliate. Mr. Eng received his J.D. from Fordham Law School in 1982 and his B.A. from Queens College in 1979.

SHERRY L. GEYER, coauthor of chapter 4, is currently a Vice President at First Republic Bank. She was formerly counsel at Reed Smith LLP in San Francisco where her practice focused on real estate and real estate finance. She represented clients in real estate acquisitions and dispositions, leasing, public and private development, and financing transactions. Ms. Geyer received her J.D. from Loyola Law School in 1988 and her B.A. from the University of California (Los Angeles) in 1971.

THEANI C. LOUSKOS, coauthor of chapter 1 is a principal with the firm of Bartko, Zankel, Tarrant & Miller, San Francisco. Ms. Louskos received her J.D. from the University of California, Berkeley, School of Law in 1980. She specializes in commercial real estate transactions, including the purchase and sale, financing, and leasing of office and retail properties. Ms. Louskos has handled major real estate acquisitions and sales on behalf of developers and REITs. She is a frequent speaker on real estate topics and served as the moderator for CEB's program on Purchase and Sales Agreements in 2002, 2004, and 2006.

LAURA S. LOWE, coauthor of chapter 15, is counsel with Miller, Starr, Regalia, Walnut Creek and was formerly the West Region Agency Counsel for LandAmerica Financial Group, Inc. Ms. Lowe was in-house counsel for the title insurance industry from 1998 to 2008. Before this she worked as a litigation attorney for various firms in the Bay Area. She is a member and past chair of the California Land Title Association's (CLTA) Education Committee. Ms. Lowe has presented programs for CEB, the Real Property Section of the State Bar of California, the National Business Institute, and the CLTA, and has provided classes to various real estate companies, mortgage loan brokerages, and local real estate organizations. She is the coauthor of two chapters in California Easements and Boundaries: Law and Litigation (Cal CEB 2008). Ms. Lowe graduated from the University of San Francisco School of Law in 1982 and received her B.S. in 1974 from Ohio State University.

PETER S. MUÑOZ, coauthor of chapter 9, is a partner with Reed Smith, LLP in San Francisco. Mr. Muñoz's clients consist of a mix of large, mid-size, and small banks, savings and loan companies, equipment leasing companies, mortgage companies, and private real estate and commercial financing entities. He generally represents creditors and lenders and equipment lessors in the documentation of complex credit transactions and in the restructuring and enforcement of such transactions both inside and outside of the bankruptcy courts. Occasionally he represents guarantors or borrowers in such transactions. He specializes in all forms of commercial and real estate finance transactions, asset-based loans, intellectual property financing, and agricultural lending. Mr. Muñoz has written and lectured extensively on issues of real and personal property lending and foreclosure, and a variety of UCC matters. He is the author of California Real Estate Finance Practice: Strategies and Forms, chap 7 (Cal CEB 2000); and he is contributing editor to California Mortgage and Deed of Trust Practice (3d ed Cal CEB 2000). Mr. Muñoz is currently a member of California Bankers Association Legal Affairs Committee and a member of the American College of Commercial Finance Lawyers. He received his J.D. from the University of California, Berkeley, School of Law.

HOWARD L. PEARLMAN, author of chapter 6, is a principal at Bartko, Zankel, Tarrant & Miller, San Francisco. Mr. Pearlman's practice focuses on real estate litigation and transactions. He has litigated, arbitrated, and mediated a wide range of disputes arising out of purchase and sale agreements, listing agreements, construction contracts, commercial leases, and condominium governing documents, as well as boundary disputes, construction defects, and nondisclosure claims. Mr. Pearlman also represents clients in environmental litigation and counsels on environmental aspects of real estate transactions. He received his J.D. from the University of California, Hastings College of the Law and his B.A. from Reed College.

SCOTT A. SOMMER, author of chapters 10, 11, and 12, is a partner at Pillsbury Winthrop Shaw Pittman, LLP, San Francisco. His practice involves complex real property matters, including land use, environmental, and land title issues. Mr. Sommer is the author of the same chapters in the second and third editions of California Real Property Sales Transactions, is a coauthor of Miller & Starr, California Real Estate (3d ed 2002), and has been a frequent speaker at continuing legal education courses sponsored by CEB. He received his J.D. degree in 1976 from the University of California, Hastings College of the Law and his B.A. degree in 1972 from the University of California (Santa Barbara).

STEVE STWORA-HAIL, coauthor of chapter 3, is a partner and chairs the Real Property Group at Downey Brand LLP, Sacramento. His transactional practice emphasizes leasing, acquisitions, financing, development, and land use. He has chaired the Real Property Section of the State Bar of California, is a past member of the Governing Committee of CEB,

and has been a contributing writer, editor, and speaker for CEB and the Real Property Law Section of the State Bar. Mr. Stwora-Hail received his B.A. degree from the University of Chicago and his J.D. from Santa Clara University.

TIMOTHY R. SULLIVAN, author of chapters 13 and 14, is of counsel with McCormick, Barstow, Sheppard, Wayte & Carruth LLP, Fresno and was formerly a partner with McLaughlin Sullivan LLP, Fresno. Mr. Sullivan represents both insurers and insureds in a variety of insurance-related matters, including bad faith and declaratory relief actions. He also defends insurance brokers and agents in malpractice cases and provides advice to business clients regarding their exposures and insurance coverages. In 2008, Mr. Sullivan was selected for inclusion as a "Super Lawyer" in Insurance Coverage. In 2007, he was appointed to the Executive Committee of the Real Property Law Section. He was elected to the Fresno County Bar Association Board of Directors, where he currently serves as First Vice-President. Mr. Sullivan is also a coauthor of California Title Insurance Practice (2d ed Cal CEB 1997) and Office Leasing: Drafting and Negotiating the Lease (Cal CEB 1996), and has just finished updating a chapter on insurance and indemnity for California Construction Contracts, Defects, and Litigation (Cal CEB 2008). He received his J.D. degree in 1986 and his B.A. degree in 1983 from the University of Missouri at Columbia.

WILLIAM D. WICK, coauthor of chapter 7, is a partner with Wactor & Wick LLP, Oakland. Mr. Wick's practice is devoted exclusively to environmental counseling and litigation, with a focus on hazardous site cleanup matters. He counsels and defends clients in real estate, regulatory, and enforcement matters, and serves as an expert witness on the law relating to hazardous site cleanup. He is "AV" rated by Martindale-Hubble (highest rating) and is rated "Superb" by avvo.com (highest rating). He has been consistently selected by other lawyers as a "Northern California Super Lawyer" in Environmental Law by Law & Politics (2005 through 2008). He is an advisor and former member of the Executive Committee of the Environmental Section of the State Bar of California, and is former Chair of the Environmental Section of the Bar Association of San Francisco. Before entering private practice in 1991, Mr. Wick served for 13 years as an enforcement attorney with the U.S. Environmental Protection Agency, where he was responsible for enforcement under all major federal statutes. He was the Chief of the Hazardous Waste Branch of the Office of Regional Counsel for Region IX for 6 years, supervising 30 attorneys responsible for hazardous site cases in Arizona, Nevada, California, Hawaii, and the Trust Territories. Mr. Wick was an Adjunct Professor at Golden Gate University School of Law, where he taught environmental law from 1981 to 1991. He is a frequent speaker and writer on environmental law topics, and has been a regular contributor to "The Practitioner" column on environmental law in the San Francisco Daily Journal and Los Angeles Daily Journal. Mr. Wick received his B.A. degree from Northwestern University in 1971 and his J.D. degree from Georgetown University Law Center in 1974.

© The Regents of the University of California

About the 2009 Update Author

RANDALL I. BARKAN, update coauthor of chapter 2; see biography in the About the Authors section of this book.

JEFFREY H. BELOTE, update coauthor of chapter 2; see biography in the About the Authors section of this book.

PETER BRIAN BOTHEL, update coauthor of chapter 15; see biography in the About the Authors section of this book.

GORDON K. ENG, update author of chapter 8; see biography in the About the Authors section of this book.

THEANI C. LOUSKOS, update coauthor of chapter 4; see biography in the About the Authors section of this book.

LAURA S. LOWE, update coauthor of chapter 15; see biography in the About the Authors section of this book.

STEVEN M. MULDOWNEY, update coauthor of chapter 5, is a partner in the Orange County office of the law firm of Cox, Castle & Nicholson LLP. Mr. Muldowney's practice is focused on the areas of acquisition, financing, development, management, and disposition of hotel and resort properties, timeshare, fractional, private residence club and condo-hotel projects, condominium projects, master planned residential communities, mixed use (residential/commercial) projects and commercial properties. Mr. Muldowney also represents lenders and borrowers in bankruptcy, foreclosure, forbearance, and other workout arrangements with regard to such properties. He has published numerous articles concerning resort and residential properties and has been a frequent guest lecturer at the University of California, Irvine and the Chapman University School of Law. Mr. Muldowney received his B.A. degree from Brown University in 1985, served as an officer in the United States Air Force from 1985 through 1992, and received his J.D. degree from the University of California, Davis, School of Law in 1995. He is a member of the American Resort Development Association, the Orange County Building Industry Association, and the Orange County Business Council.

PETER S. MUÑOZ, update coauthor of chapter 9; see biography in the About the Authors section of this book.

HOWARD L. PEARLMAN, update author of chapter 6; see biography in the About the Authors section of this book.

SCOTT A. SOMMER, update author of chapters 10, 11, and 12; see biography in the About the Authors section of this book.

ARTHUR O. SPAULDING, JR., update coauthor of chapter 5, is the managing partner of the Irvine office of Cox, Castle & Nicholson LLP. Mr. Spaulding is a senior transactional real estate attorney with extensive experience in the acquisition, disposition, financing, and development of real estate projects, specializing in matters involving hotel and resort ownership. Representing both developers and lenders, he has been actively involved in multiple facets of the acquisition, management, ownership, and financing of hotels and resorts, both in California and otherwise (including significant experience with properties in Mexico, Fiji, the British Virgin Islands, and the Caymans). He has lectured widely in the field of hospitality development, and has spoken at the NYU and UCLA Hotel Industry Investment Conferences, the Lodging Conference in Scottsdale, Arizona, and the International Law Symposia on resort development sponsored jointly by the American Bar Association and the International Bar Association held in Marbella, Spain and Los Angeles, California. Mr. Spaulding also specializes in matters involving timesharing and vacation ownership and serves as a Trustee for the American Resort Development Association. He has served two terms as a member of the ARDA Board of Directors and is the immediate past-Chairman of the ARDA Ethics Committee.

STEVE STWORA-HAIL, update author of chapter 3; see biography in the About the Authors section of this book.

TIMOTHY R. SULLIVAN, update author of chapters 13 and 14; see biography in the About the Authors section of this book.

WILLIAM D. WICK, update author of chapter 7; see biography in the About the Authors section of this book.

SARA HANSEN WILSON, update author of chapter 1, is a partner in the San Francisco office of Drinker Biddle & Reath, LLP. She focuses her practice on leasing, acquisitions and dispositions, and financing commercial real estate properties. Ms. Wilson received her J.D. from the University of California, Los Angeles, School of Law and her B.A. from Williams College. She is a frequent speaker on commercial real estate topics for various organizations, including CEB, the International Council of Shopping Centers Law Conference, ALI-ABA, Practising Law Institute, and CLE International.

© The Regents of the University of California

Selected Developments

December 2009 Update

Lawyer's Role:

Attorneys must notify their clients in writing if they do not maintain professional liability insurance. Cal Rules of Prof Cond 3-410. See §1.12A.

Brokers:

As of December 1, 2010, California real estate brokers acting as mortgage loan originators will be required to obtain a real estate license endorsement and to register on the National Mortgage Licensing System and Registry. Fin C §22100. See §2.7.

In response to the increasing number of loan modification and foreclosure rescue scams in California, AB 260 and SB 94 added a number of new laws affecting mortgage brokers. See §2.8B.

In *RC Royal Dev't and Realty Corp. v Standard Pac. Corp.* (Sept. 29, 2009, B206894) 2009 Cal App Lexis 1606, the court held that a provision in an agency agreement stating that the commission would be paid at closing merely designated the timing of the payment and the close of escrow was not a condition precedent to payment. See §2.110.

Purchase Agreements:

In *Peak-Las Positas Partners v Bollag* (2009) 172 CA4th 101, 90 CR3d 775, the court found a seller acted in bad faith by not extending escrow on a land sale contract after the buyer had paid most of the purchase price, invested heavily in project costs, and was diligently trying to complete sale conditions. See §§4.3, 4.149, 6.21, 15.59, 15.97.

A purchase contract that allows the buyer to waive the recording of the final map is void at inception. *Sixells, LLC v Cannery Bus. Park* (2008) 170 CA4th 648, 88 CR3d 235. See §§4.92, 10.76, 11.24.

In a specific performance action, the seller is not entitled to interest on the sale proceeds if the property was overencumbered, because the entire purchase price would have been used to pay off existing liens. *Kassir v Zahabi* (2008) 164 CA4th 1352, 80 CR3d 1. See §4.149.

Civil Code §1675 was amended effective January 1, 2009, to limit the applicability of liquidated damages provisions in the sale of certain residential condominium units. See §6.14.

The court in *Thompson v Toll Dublin, LLC* (2008) 165 CA4th 1360, 81 CR3d 736 held that certain arbitration provisions in preprinted documents were procedurally and substantively unconscionable. See §6.15.

When a seller or broker is making disclosures regarding the condition of the property, whether information is sufficiently material to effect the value or desirability of property is generally a question of fact. *Calemine v Samuelson* (2009) 171 CA4th 153, 89 CR3d 495. See §§2.127, 6.31, 6.32A.

Under Civil Code §1103.4(c)(3), when making natural hazard disclosures on the statutorily mandated Natural Hazard Disclosure Statement under specified circumstance, the transferor must provide a "Notice of Right to Farm." See §6.49.

The discussions regarding deeds in lieu of foreclosure and short sales have been enhanced. See §§6.106B-6.106C.

The Mortgage Forgiveness Debt Relief Act of 2007 (Pub L 110-142) provided that in a short sale, a discharge of indebtedness income will not be taxed if the property sold is the taxpayer's principal residence, the debt is "qualified principal residence indebtedness," and the debt discharge (up to certain maximum amounts) occurred between January 1, 2007 and January 1, 2013. See §6.106C.

Until January 1, 2014, beneficiaries of deeds of trust must prepare and deliver a short-pay demand statement within 21 days of receiving a short-pay request from an entitled person or a written statement indicating that it has elected not to proceed with the transaction. CC §2943.

Under the Home Equity Sales Contracts Act, "equity purchasers" do not include persons who purchase the property for use as a personal residence, or who acquire title by deed in lieu, trustee's sale, or other statutory sale, by order or judgment of a court, or from a spouse, blood relative, or blood relative's spouse. *Spencer v Marshall* (2008) 168 CA4th 783, 85 CR3d 752. See §6.107.

The discussion regarding the sale of bank-owned property, commonly known as REO sales, has been enhanced. See §6.110.

Hazardous Waste:

The Supreme Court in *Burlington N. & Santa Fe Ry. Co. v U.S.* (2009) 556 US __, 173 L Ed 2d 812, 129 S Ct 1870 has held that apportionment among defendants is proper if there is a reasonable basis for determining the contribution of each defendant to a single harm. See §7.10.

Options:

In *Patel v Liebermensch* (2008) 45 C4th 344, 86 CR3d 366, the California Supreme Court discussed specific performance of a real estate option contract and held that the time of payment may be implied, using the custom and intent of the parties and other terms of the contract. See §§4.4, 6.5, 8.9.

Seller Financing:

Garcia v Roberts (2009) 173 CA4th 900, 93 CR3d 286 illustrates fraudulent use of the lease-option device. See §9.19.

Deeds, Property Descriptions, Easements, Dedications:

The deed's description of the form of title is presumed to reflect the actual ownership interest in the property, rebuttable only by clear and convincing proof. *Marriage of Brooks & Robinson* (2008) 169 CA4th 176, 184, 86 CR3d 624.

In *Lee v Lee* (2009) 175 CA4th 1553, 1558, 97 CR3d 516 the court held that a deed altered after execution is not void. See §10.76.

A restriction on resale price contained in prior recorded covenants, conditions, and restrictions (CC&Rs) could be enforced against a purchaser in an affordable housing development, in the absence of duress or fraud. See *Alfaro v Community Housing Improvement Sys. & Planning Ass'n* (2009) 171 CA4th 1356, 89 CR3d 659. See §§11.7, 11.11, 11.75.

In *Gray v McCormick* (2009) 167 CA4th 1019, 84 CR3d 777, exclusive easement language in a subdivision's CC&Rs was held enforceable as to the surface of the land, which was the servient tenement. See §11.52.

The easement claimant bears the burden of producing evidence to overcome the inference caused by the omission of an express reservation of a right of access to such property. See *Murphy v Burch* (2009) 46 C4th 157, 167, 92 CR3d 381. See §11.56.

A court has equitable power to allow a historic road to continue to encroach even though a prescriptive easement of necessity is not cognizable. See *Linthicum v Butterfield* (2009) 175 CA4th 259, 265, 95 CR3d 538. See §11.57.

Although a grant in fee simple without an express covenant is sufficient to pass the grantor's after-acquired title, a quitclaim deed transfers only the interest that the transferor has at the date of its execution and thus does not transfer an after-acquired title. See *Johnson v E-Z Ins. Brokerage, Inc.* (2009) 175 CA4th 86, 94, 95 CR3d 782. See §§10.4, 12.10.

For a discussion of appropriative water rights that are appurtenant and run with the land, see *Nicoll v Rudnick* (2008) 160 CA4th 550, 558, 72 CR3d 879. See §10.44.

Insurance:

In *Major v Western Home Ins. Co.* (2009) 169 CA4th 1197, 87 CR3d 556, the court describes the type of testimony, which would support a plaintiff's claim for apportioned fees and costs. The court of appeal also listed factors that qualified a claims agent as a managing agent (for purposes of corporate bad faith) and noted that the payment of legal fees and court cost to enforce a claim under the policy may satisfy the requirement of economic loss for recovery of emotional distress damages. See §§13.114-13.115, 13.117.

The court in *Exxon Shipping Co. v Baker* (2008) __ US __, 171 L Ed 2d 570, 128 S Ct 2605 distinguished the "more rigourous standards than the constitutional limit on punitive damages" that apply to jury awards under maritime law. See §13.118.

In *Freedman v State Farm Ins. Co.* (2009) 173 CA4th 957, 93 CR3d 296, the appellate court held that even though the "all risk" policy included mold, the damages were not covered, because caused by excluded third party negligence, corrosion, and continuous or repeated seepage or leakage of water. See §§13.72, 13.83, 13.86, 13.131.

If disputed, the termination of the "period of restoration" is a question of fact. See *Shaw Mortgage Corp. v Peerless*

Ins. Co. (SD Cal 2009) 615 F Supp 2d 1172; *R&R Sails, Inc. v Insurance Co. of the State of Pennsylvania* (SD Cal 2009) 610 F Supp 2d 1222. See §13.60.

Brehm v 21st Century Ins. Co. (2008) 166 CA4th 1225, 83 CR3d 410 holds that both good faith subjective intent and objectively reasonable conduct are necessary to defeat a bad faith claim on demurrer. However, the court of appeal in *Bosetti v U.S. Life Ins. Co. in City of New York* (2009) 175 CA4th 1208, 96 CR3d 744 holds that subjective bad faith is both insufficient and unnecessary, because "the covenant of good faith can be breached for objectively unreasonable conduct, regardless of the actor's motive." See §13.112.

Although an insurer may be estopped from relying on the statute of limitations if the insured establishes reasonable reliance, communications after the limitations period expired may not form the basis for estoppel. See *Shugerman v Allstate Ins. Co*. (CD Cal 2009) 594 F Supp 2d 1131. See §§13.93, 13.95-13.96.

In *McCoy v Progressive W. Ins. Co*. (2009) 171 CA4th 785, 90 CR3d 74 the court of appeal affirmed the trial court's refusal to instruct that a "genuine dispute" precludes bad faith, because that doctrine is subsumed within the concept of reasonableness. See §13.120.

The supreme court held that the Consumer Legal Remedies Act (CC §§1750-1784) does not apply to life insurance because it is not a "good" or "service" in *Fairbanks v Superior Court* (2009) 46 C4th 56, 92 CR3d 279. Also see *Broberg v The Guardian Life Ins. Co. of Am.* (2009) 171 CA4th 541, 79 CR3d 721. See §13.123.

In *Delgado v Interins. Exch. of the Auto. Club of S. Cal.* (2009) 47 C4th 302, 97 CR3d 298, the supreme court held that an insured's unreasonable belief in the need for self-defense does not turn an assault and battery into an accident. See §14.18.

An "extended reporting period" may not apply to a claim made against the insured during the original policy period. See *World Health & Education Foundation v Carolina Cas. Ins. Co.* (ND Cal 2009) 612 F Supp 2d 1089. See §14.13, 14.15.

The Consumer Product Safety Commission has received more than 800 complaints from 23 states concerning drywall imported from China since 2006. These complaints of property damage and illness raise numerous insurance issues that have not yet been resolved. See §§13.137-13.141.

Escrow:

The issuance, transfer, or exchange of a security or the making or delivery of an instrument of transfer pursuant to a plan confirmed under Bankruptcy Code, Chapter 11 is exempt from state or local transfer taxes. 11 USC §1146(a). The transfer tax exemption applies only to transfers made pursuant to a confirmed Chapter 11 plan. See *Florida Dep't of Revenue v Piccadilly Cafeterias, Inc.* (2008) ___ US ___, 171 L Ed 2d 203, 128 S Ct 2326. See §4.134.

The Department of Housing and Urban Development promulgated new rules under the Real Estate Settlement Procedures Act designed to require more timely and effective disclosure of settlement costs in order to make the mortgage financing process clearer and less costly to consumers. See 73 Fed Reg 68204 (2008) and §§6.23, 15.95.

© The Regents of the University of California

Cutoff Dates and CEB Citation

Cutoff Dates

We completed legal editing and analysis of authorities cited in this publication as of August 14, 2009, and monitored developments through October 12, 2009.

CEB Citation

Cite this publication as: California Real Property Sales Transactions (4th ed Cal CEB 2007).

© The Regents of the University of California

1

Lawyer's Role in Real Property Sales

I. INTRODUCTION §1.1

II. OVERVIEW OF ATTORNEY'S ROLE
- A. Services Typically Provided by Attorney §1.2
- B. Professional Responsibility §1.3
  - 1. Rules of Professional Conduct §1.4
    - a. General Standard of Performance §1.5
    - b. Conflicts and Financial Relationships §1.6
      - (1) Conflict With Attorney's Own Interest §1.7
      - (2) Conflict With Other Interests §1.8
        - (a) Written Disclosure §1.9
        - (b) Informed Written Consent §1.10
        - (c) Risks of Multiple Representation §1.11
      - (3) Handling Client's Property §1.12
    - c. Professional Liability Insurance §1.12A
  - 2. Malpractice Law §1.13
    - a. Duty of Care §1.14
    - b. Fiduciary Duty §1.15
  - 3. Resource Materials on Malpractice §1.16
- C. Defining the Engagement
  - 1. Clearly Communicating Scope and Content of Engagement §1.17
  - 2. Piecemeal Involvement §1.18
- D. Defining the Fee
  - 1. The Fee Agreement §1.19
  - 2. Amount of Fee §1.20
  - 3. Equity Interests §1.21

III. IDENTIFYING CLIENT'S NEEDS AND OBJECTIVES
- A. Needs and Objectives as Important Guideposts §1.22
- B. Areas to be Explored With Client
  - 1. Client's Purpose in Selling or Buying the Property §1.23
    - a. Seller's Objectives §1.24
    - b. Purchaser's Objectives §1.25
  - 2. Alternatives to Sale §1.26
    - a. Seller's Alternatives
      - (1) Leasing Transaction §1.27
      - (2) Other Sources of Liquidity §1.28
        - (a) Debt Sources §1.29
        - (b) Equity Sources §1.30
      - (3) Development of the Property in Furtherance of Sale §1.31
      - (4) Other Sources of Relief §1.32
    - b. Purchaser's Alternatives §1.33
      - (1) Leasing Transaction §1.34
      - (2) Other Equity Transactions §1.35
    - c. The "Go/No-Go" Alternative §1.36
  - 3. Client's Timing Needs §1.37
    - a. Ascertaining Client's Needs §1.38
    - b. Degree and Causes of Any Timing Requirements §1.39
      - (1) Seller Timing Requirements §1.40
      - (2) Purchaser Timing Requirements §1.41
  - 4. Net Proceeds Requirements §1.42
    - a. The Bottom Line §1.43
    - b. Distinguishing Between Wants and Needs §1.44
      - (1) Wants §1.45
      - (2) Needs §1.46
  - 5. Client's Risk Tolerance: Presale Contingencies §1.47

a. Seller's Presale Risk Tolerance §1.48
b. Purchaser's Presale Risk Tolerance §1.49
6. Client's Risk Tolerance: Postsale Contingencies §1.50
a. Seller Financing §1.51
b. Condition of Property §1.52
c. Other Postsale Problems §1.53
7. Client's Tax and Financial Accounting Requirements §1.54
8. Client's Knowledge and Experience Concerning the Property
a. Seller's Knowledge and Experience §1.55
b. Purchaser's Knowledge and Experience §1.56
9. Client's Transactional Resources §1.57

IV. PRECONTRACT DUE DILIGENCE §1.58
A. Precontract Due Diligence Matters to Review With Seller
1. Seller's Objectives §1.59
2. Consider Valuation of Property §1.60
3. Review Condition of Title §1.61
4. Review Condition of Property
a. Existing Information §1.62
b. Additional Information §1.63
c. Special Situation: Environmental Conditions §1.64
5. Review Legal Issues Affecting Property §1.65
6. Ascertain Whether Consents Needed From Others
a. Internal Approvals §1.66
b. External Approvals and Nonobjections §1.67
7. Review Matter From Purchaser's Perspective §1.68
8. Assist in Engaging Outside Experts §1.69
B. Precontract Due Diligence Matters to Review With Purchaser
1. Purchaser's Objectives §1.70
2. Financing the Purchase §1.71
3. Legal Feasibility of Intended Use
a. Necessary Approvals §1.72
b. Effect of Applicable Laws §1.73
(1) Local and Regional Laws §1.74
(a) General Plans §1.75
(b) Specific Plans §1.76
(c) Zoning Ordinances §1.77
(d) Building Codes §1.78
(e) Subdivision Approvals §1.79
(f) Miscellaneous Applicable Laws §1.80
(2) State Laws §1.81
(a) Environmental Laws §1.82
(b) Subdivision Map Act §1.83
(c) Laws on Vested Rights §1.84
(d) Laws Regulating Foreign Investment and Disposition §1.85
(e) Miscellaneous Applicable Laws §1.86
(3) Federal Laws §1.87
(a) Environmental Laws §1.88
(b) Laws Regulating Foreign Investment and Disposition §1.89
(c) Miscellaneous Applicable Laws §1.90
4. Economic Feasibility of Intended Use §1.91
5. Consents Needed From Others §1.92
6. Assist in Engaging Outside Experts §1.93

V. STRUCTURING THE TRANSACTION §1.94
A. Structuring Seller/Purchaser Entities
1. Advising the Seller §1.95
2. Advising the Purchaser §1.96
B. Structuring the Transaction Itself §1.97
1. Choice of Form §1.98
2. Liquidated Damages §1.99
3. Warranties §1.100
4. Tax-Deferred Exchange §1.101
5. Letter of Intent §1.102
6. Client's Ability to be Flexible §1.103

VI. STRUCTURING AND COORDINATING THE MARKETING PROCESS
A. Marketing Considerations to Review With Seller §1.104
1. Brokered or Nonbrokered Sale §1.105
2. Negotiated Sale or Sale Involving Bidding
a. Estate §1.106
b. Nonestate §1.107
3. Anticipating Multiple Offers §1.108
B. Marketing Considerations to Review With Purchaser §1.109
1. Separate Broker §1.110
2. Negotiated Sale Versus Bidding Sale
a. Estate §1.111
b. Nonestate §1.112
3. Anticipating Multiple Offers §1.113

VII. STRUCTURING AND COORDINATING THE NEGOTIATION AND DOCUMENTATION PROCESS §1.114
A. Organizing the Negotiating Team §1.115
B. Conducting Negotiations §1.116
1. Other Counsel §1.117
2. Attorney's Role in Negotiation Process §1.118
C. Generating Transactional Documents
1. Drafting and Adapting Forms §1.119
2. Standard Forms; Boilerplate §1.120
D. Rendering Legal Opinions
1. Contexts in Which Legal Opinions Arise §1.121
2. How to Know an Opinion When You See One §1.122
a. Watch for Writings in Legal Opinion Contexts §1.123
b. Watch for "Factual," "Reasoned," and "Comfort" Opinions §1.124
c. Avoid Unnecessary Opinions §1.125
3. Legal Standards Applicable to Opinions §1.126
4. Essential Resources Available to the Attorney §1.127
a. State Bar Reports §1.128
b. ABA Reports §1.129
c. Accord §1.130

VIII. STRUCTURING AND COORDINATING THE CLOSING PROCESS
A. Organizing and Coordinating Escrow
1. Understanding the Process §1.131
2. Written Escrow Instructions; Follow-Up §1.132
B. Advising Client on Title Insurance §1.133
1. Choice of Basic Policy Forms §1.134
2. Addressing Particular Problems §1.135
3. Policy Endorsements §1.136
4. Wording of Policy Provisions §1.137
5. Insurer's Financial Ability §1.138
6. Policy Costs and Required Lead Times §1.139

IX. POSTCLOSING FOLLOW-UP
A. Making Sure All Closing Details Are Complete and Correct §1.140
B. Examples of Follow-Up Matters §1.141
1. Receipt and Review of Title Policy §1.142
2. Receipt and Review of Other Closing Documents §1.143
3. Monitoring Certain Postclosing Notices and Actions §1.144

© The Regents of the University of California

§1.1 I. INTRODUCTION

This chapter discusses the various ways the lawyer can be effective in assisting a client throughout the successive stages of a real property purchase and sale transaction. To get the most out of this chapter, think of it as two things: a discussion of practical steps that will be helpful in working through actual transactions, and an introductory discussion of concepts that will serve as a framework on which the later chapters in this book will build. As a further practice aid, the following sections are organized in a manner that should make the outline at the beginning of this chapter useful as a transaction checklist.

© The Regents of the University of California

II. OVERVIEW OF ATTORNEY'S ROLE

§1.2 A. Services Typically Provided by Attorney

The lawyer's role in a real estate transaction will vary widely, depending on the complexity of the transaction, the real estate experience of the seller and the purchaser, the stage at which the attorney's assistance is sought, and whether the property is commercial or residential. Many sellers and purchasers who are experienced in the acquisition and sale of real property may engage counsel for very limited purposes; for example, to draft a purchase agreement for the seller, or to review a buyer's comments to the seller's purchase agreement and to advise the seller as to acceptable changes, or to review the title condition of the property for the purchaser. If either of the parties is inexperienced, the lawyer may have a more extensive role in the transaction.

The lawyer can assist the client in a variety of ways throughout the various stages of the transaction, including:

- Bringing a focus to the client's needs and objectives;
- Helping formulate and implement presale/prepurchase due diligence;
- Structuring the transaction; and
- Assisting with the marketing process, negotiating and drafting the documents, the closing process, and postclosing follow-up.

In preliminary discussions with the client, the lawyer should make sure that the client understands the full range of services that the lawyer can provide. Although a lawyer may not be involved in every aspect of the transaction, the balance of this chapter describes how the lawyer can assist his or her client at each stage.

Before turning to the specifics of the lawyer's role, it is first necessary to be clear about two aspects of the lawyer's involvement that will be fundamental to the lawyer-client relationship, regardless of the lawyer's role in the transaction: the lawyer's professional responsibility to the client (§§1.3-1.16) and the steps to take in defining the engagement (§§1.17-1.18).

© The Regents of the University of California

§1.3 B. Professional Responsibility

The basic rules of professional responsibility are the same in real property transactions as in other transactions. It is sobering to reflect, however, that the number of claims based on breaches of these rules is statistically higher in real property practice than in most other practice areas. Data collected by the ABA National Legal Malpractice Data Center indicate that lawyers practicing personal injury law, real estate, and family law are the practitioners most likely to have claims brought against them for legal malpractice. Collectively, claims in these areas accounted for nearly 56 percent of all legal malpractice claims brought between 2000 and 2003. Profile of Legal Malpractice Claims: 2004-2007, ABA Standing Committee on Lawyers' Professional Liability (Sept. 2008).

However, the ABA's statistical analysis reflects a decline in recent years in real estate malpractice claims: the absolute number of such filings decreased from 6253 to 4879 during the 1999-2003 survey period. ABA Profile, p 3. The real property lawyer's relative share of malpractice claims has also declined slightly during that period: real estate accounted for 16.46 percent of all malpractice claims in 2003 as compared to 16.97 percent in 1999. Because of the limitations on the collection of these data, it is unclear whether the number of claims at present is disproportionate to the overall time spent by lawyers in this practice area. Nonetheless, the continuing statistical prominence of real estate malpractice claims should serve as an instructive reminder that conscientious attention should be paid to the rules of professional responsibility in real property practice. For information on how to obtain a copy of the study, see the Directory.

© The Regents of the University of California

§1.4 1. Rules of Professional Conduct

The Rules of Professional Conduct of the State Bar of California are formulated by the Board of Governors subject to the approval of the California Supreme Court. Bus & P C §6076. The Rules govern the activities of State Bar members in and outside of California, except to the extent that members lawfully practicing outside of California may be specifically required by the jurisdiction in which they are practicing to follow different rules of professional conduct. Cal Rules of Prof Cond 1-100(D)(1). The Rules also govern the activities of nonmember lawyers while they are performing lawyer functions in this state, but the Rules do not authorize the performance of those functions by nonmembers except as otherwise permitted by law. Cal Rules of Prof Cond 1-100(D)(2). For assistance in researching specific ethics issues, and for up-to-the-minute information on the Rules currently in effect (as well as any amendments or additions being proposed), a convenient source is the State Bar's Ethics Hotline. See Directory for telephone number.

The lawyer's ethical responsibilities to the client in a real property transaction, as in any client matter, are governed by the Rules. Every lawyer should, of course, be generally familiar with all of them. In addition, the areas covered by the Rules and discussed in §§1.5-1.12 merit particular emphasis.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/1 Lawyer's Role in Real Property Sales/§1.5 a. General Standard of Performance

§1.5 a. General Standard of Performance

A general standard of performance is set forth in Cal Rules of Prof Cond 3-110. This Rule provides that a member "shall not intentionally, recklessly, or repeatedly fail to perform legal services with competence." Rule 3-110(A). For purposes of the Rule, "competence" in any legal service means "to apply the 1) diligence, 2) learning and skill, and 3) mental, emotional, and physical ability reasonably necessary for the performance of such service." Rule 3-110(B).

© The Regents of the University of California

§1.6 b. Conflicts and Financial Relationships

Three additional rules address circumstances that often occur in real property transactions. One circumstance arises when the lawyer has an opportunity to invest or otherwise participate financially in a project with the client. See §1.7. Another circumstance arises when a current client's interests potentially or actually conflict with the interests of another client or former client. See §§1.8-1.11. The third circumstance arises when the lawyer is asked to handle money or other property belonging to the client. See §1.12.

© The Regents of the University of California

§1.7 (1) Conflict With Attorney's Own Interest

Under Cal Rules of Prof Cond 3-300, a member is prohibited from entering into a business transaction with a client or knowingly acquiring an ownership, or a possessory, security, or other pecuniary interest adverse to the client unless three rigorous requirements of the rule are satisfied:

- The transaction and its terms are fair and reasonable to the client and are fully disclosed and transmitted in writing to the client in a manner that should reasonably be understood by the client;
- The client is advised in writing that the client may seek the advice of an independent lawyer of the client's choice and is given a reasonable opportunity to seek that advice; and
- The client thereafter consents in writing to the terms of the transaction.

See *In re Casey* (2008) 4 Cal St Bar Ct Rptr 11237, 2008 Cal Op Lexis Ct 3.

A member is prohibited from directly or indirectly purchasing property at a probate, foreclosure, receiver's, trustee's, or judicial sale in an action or proceeding in which "such member or any lawyer affiliated by reason of personal, business, or professional relationship with that member or with that member's law firm is acting as a lawyer for a party or as executor, receiver, trustee, administrator, guardian, or conservator." Cal Rules of Prof Cond 4-300(A). Under Cal Rules of Prof Cond 4-300(B) a member is prohibited from representing the seller at a probate, foreclosure, receiver's, trustee's, or judicial sale in which the purchaser "is a spouse or relative of the member or of another lawyer in the member's law firm or is an employee of the member or the member's law firm."

© The Regents of the University of California

§1.8 (2) Conflict With Other Interests

California Rules of Professional Conduct 3-310 applies to a variety of circumstances in which the lawyer's existing or contemplated representation of a client may involve an actual or a potential conflict of the client's interest with the interests of other persons or entities with whom the lawyer has or has had a relationship.

© The Regents of the University of California

§1.9 (a) Written Disclosure

Under Cal Rules of Prof Cond 3-310(B), a member is prohibited from accepting or continuing representation of a client without providing written disclosure to the client in these situations:

- The member has a "legal, business, financial, professional, or personal relationship" with a party or witness in the same matter;
- The member knows or reasonably should know that he or she previously had such a relationship with a party or a witness in the same matter and that such previous relationship would substantially affect the member's representation of the client in the present matter;
- The member has or had such a relationship with another person or entity that the member knows or reasonably should know would be affected substantially by resolution of the matter; or
- The lawyer has or had a "legal, business, financial, or professional interest in the subject matter of the representation."

"Written" means any writing as defined in Evid C §250 (Cal Rules of Prof Cond 3-310(A)(3)), which has been expanded to include photocopies, e-mails, and faxes, and any record "thereby created" "regardless of the manner in which the record has been stored."

"Disclosure" means informing the client or former client of "the relevant circumstances and of the actual and reasonably foreseeable adverse consequences" of the conflicting relationship or interest. Cal Rules of Prof Cond 3-310(A)(1).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/1 Lawyer's Role in Real Property Sales/§1.10 (b) Informed Written Consent

§1.10 (b) Informed Written Consent

"Informed written consent" means the client's or former client's "written agreement to the representation following written disclosure." Cal Rules of Prof Cond 3-310(A)(2). Under Cal Rules of Prof Cond 3-310(C), the informed written consent of each client must be obtained before a member may

- accept representation of more than one client in a matter in which the clients' interests potentially conflict;
- accept or continue representation of more than one client in a matter in which the clients' interests actually conflict; or
- represent a client in one matter and at the same time in a separate matter accept representation of another client who has an interest in the first matter adverse to the first client.

California Rules of Professional Conduct 3-310 also requires each client's informed written consent before a member may

- represent multiple parties to an aggregate settlement of claims of or against the parties (Cal Rules of Prof Cond 3-310(D)); or
- accept employment adverse to a client or former client when the member has obtained confidential information material to the employment through his or her representation of the client or former client (Cal Rules of Prof Cond 3-310(E)).

Rule 3-310 also prohibits attorneys from accepting compensation for representing a client from someone other than the client unless the Rule's specific requirements are met. See Cal Rules of Prof Cond 3-310(F).

© The Regents of the University of California

§1.11 (c) Risks of Multiple Representation

Particularly in small transactions, both purchaser and seller may want to rely on the same lawyer for advice and even drafting. It is improper under the Rules to represent both parties unless the lawyer has disclosed to each party in writing the lawyer's representation of the adverse interest and obtained their informed written consent. Cal Rules of Prof Cond 3-310(C)(1). If multiple representation is undertaken and an actual conflict arises, the lawyer cannot continue representing the multiple clients without further informed written consent. Cal Rules of Prof Cond 3-310(C)(2). If multiple representation is not continued, it is likely that further informed written consent will be required by Cal Rules of Prof Cond 3-310(E) (or by principles existing outside the disciplinary context, *e.g., Woods v Superior Court* (1983) 149 CA3d 931, 197 CR 185) before the lawyer may continue representing any of the clients in the matter. Violation of these principles may render the lawyer civilly liable as well as subject to discipline by the State Bar. See *Klemm v Superior Court* (1977) 75 CA3d 893, 142 CR 509. Even if it appears desirable for the lawyer to represent more than one party, and written disclosure is made to each party and the informed written consent of each is obtained, problems may still arise over whether the import of the consent was communicated adequately. See, *e.g., Hawkins v State Bar* (1979) 23 C3d 622, 153 CR 234.

PRACTICE TIP: The safest course is to decline to represent more than one of two or more adverse parties and to suggest that the other party or parties obtain separate counsel. In some situations, the representation of more than one party might not be immediately apparent, such as representing both a limited partnership and its general partner in a transaction in which their interests are not aligned.

© The Regents of the University of California

§1.12 (3) Handling Client's Property

Detailed requirements that must be observed in handling a client's property are set forth in Cal Rules of Prof Cond 4-100. The Rule requires, among other things, that all client funds be deposited in one or more identifiable trust accounts. The Rule proscribes the commingling of clients' funds and the lawyer's funds except under very limited, temporary circumstances. The Rule also requires prompt client notification of the receipt of the client's funds or other property, sets forth requirements on the identification and safekeeping of client property and the payment or delivery of client funds or other property as requested by the client, and sets forth requirements for the maintenance and retention of records regarding client funds and other property and the rendering of accounts to the client. Under the Rule, the Board of Governors has authority to adopt standards from time to time as to what "records" must be maintained to comply with the Rule. A set of standards was adopted by the Board effective January 1, 1993, and has not been changed.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/1 Lawyer's Role in Real Property Sales/§1.12A c. Professional Liability Insurance

§1.12A c. Professional Liability Insurance

As of January 1, 2010, an attorney must disclose in writing the absence of professional liability insurance directly to a client at the outset of the attorney-client relationship whenever it is reasonably foreseeable that the total amount of the member's legal representation of the client in the matter will exceed 4 hours. An attorney who fails to provide this notice must inform the client in writing within 30 days of the date that the attorney subsequently knows or should know that he or she no longer has professional liability insurance. Cal Rules of Prof Cond 3-410.

© The Regents of the University of California

§1.13 2. Malpractice Law

The law of malpractice imposes two basic duties on the lawyer. One is a general duty of care, *i.e.,* to perform legal services competently and free from negligence. See §1.14. The other is a fiduciary duty that arises from the lawyer-client relationship. See §1.15.

© The Regents of the University of California

§1.14 a. Duty of Care

The duty of care is the duty to perform the service for which the lawyer has been retained with "such skill, prudence, and diligence as other members of his profession commonly possess and exercise in the performance of the tasks which they undertake." Prosser, Law of Torts (4th ed. 1971) §30 at 143 as quoted in *Lucas v Hamm* (1961) 56 Cal 2d 583, 591, 15 CR 821; *Budd v Nixen* (1971) 6 C3d 195, 98 CR 849; *Dawson v Toledano* (2003) 109 CA4th 387, 396, 134 CR2d 689. The duty encompasses both a knowledge of law and an obligation of diligent research and informed judgment. *Janik v Rudy, Exelrod & Zieff* (2004) 119 CA4th 930, 936, 14 CR3d 751. In areas of specialty, of which real property law appears to be one (see, *e.g.,* discussion of specialized practice areas in Committee on Specialization, Results of Survey on Certification of Specialists, 44 SBJ 140 (1969)), there are significant refinements to that general statement of the lawyer's duty. A lawyer who claims to be a specialist will be held to the same standards of skill, prudence, and diligence exercised by other specialists of ordinary skill and capacity specializing in the same field. *Wright v Williams* (1975) 47 CA3d 802, 810, 121 CR 194. A lawyer who does not purport to be a specialist nevertheless must satisfy specialist standards when practicing in specialized areas. The basic choices open to a nonspecialized lawyer are either to refer the specialty issues to a specialized practitioner or, if the lawyer handles the issues personally, to do so in accordance with the higher standards applicable to specialists in good standing in the same or similar locality and under the same circumstances. See *Lewis v State Bar of Cal*. (1981) 28 C3d 683, 170 CR 634.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/1 Lawyer's Role in Real Property Sales/§1.15 b. Fiduciary Duty

§1.15 b. Fiduciary Duty

Along with the duty of care, the lawyer's other basic duty is to observe the fiduciary obligations arising from the lawyer-client relationship. Stated briefly, these obligations are undivided loyalty and confidentiality. 2 Mallen & Smith, Legal Malpractice, chap 15 (2008 ed). Stated more fully (*Day v Rosenthal* (1985) 170 CA3d 1125, 1143, 217 CR 89, quoting *Betts v Allstate Ins. Co.* (1984) 154 CA3d 688, 715, 201 CR 528):

> [I]t is an attorney's duty to "protect his client in every possible way," and it is a violation of that duty for the attorney to "assume a position adverse or antagonistic to his client without the latter's free and intelligent consent given after full knowledge of all the facts and circumstances". The attorney is "precluded from assuming any relation which would prevent him from devoting his *entire* energies to his client's interest."

This duty extends only to the client and not to a party whose position is actually or potentially adverse to the lawyer's client. *B.L.M. v Sabo & Deitsch* (1997) 55 CA4th 823, 64 CR2d 335.

© The Regents of the University of California

§1.16 3. Resource Materials on Malpractice

For helpful general discussions of the law of malpractice, see Dunlavey, *Legal Malpractice: The Standards of Care,* 4 LA Law 34 (Jan. 1982), and the cases collected in Appendix B of the 1989 Report of the Committee on Corporations of the Business Law Section of the State Bar of California Regarding Legal Opinions in Business Transactions, reprinted in 45 Bus Law 2169 (1990) (see §1.28).

For an extensive treatment of the subject, including discussion of the relationship between ethical rules and the law of malpractice, see Mallen & Smith, Legal Malpractice (2008 ed).

© The Regents of the University of California

C. Defining the Engagement

§1.17 1. Clearly Communicating Scope and Content of Engagement

Regardless of the scope of the engagement, a clear, thorough communication must be conveyed to the client about the scope and content of the lawyer's role in the particular transaction. If other experts will also be involved, this step includes defining each party's role and clarifying what responsibility (if any) the lawyer will have for coordinating the work of other experts or reviewing the results of their work. If it later becomes necessary to assess the lawyer's performance, the essential cornerstone of that evaluation will be a clear understanding of what the lawyer was specifically engaged to do. Communications defining the engagement generally may be written or oral, although in conflict situations covered by the Rules of Professional Conduct discussed above, at least some writing will be required. See §§1.6-1.12. A writing may be either required or highly desirable in connection with fee arrangements. See §§1.19-1.21.

For further discussion of determining the lawyer's scope of representation regarding title insurance matters, see California Title Insurance Practice §§2.1-2.3 (2d ed Cal CEB 1997).

© The Regents of the University of California

§1.18 2. Piecemeal Involvement

The parties in a real property transaction often wish to confine their consultation with a lawyer to questions about particular clauses or to a "quick look" at the contract to identify any "big problems." This desire may partly stem from the abundance of apparently "standard" preprinted transaction forms, or it may simply be due to an understandable desire to minimize transaction costs. Whatever the reason, approach such requests with extreme caution. Frequently, the sophistication of the client and the nature of the issue on which the client has asked advice are such that discrete transactional issues can be addressed. In such situations, it is good practice to advise the client in a writing that identifies the issue or issues involved and then specifically notes the limitations on the lawyer's engagement. Piecemeal involvement that cannot be clearly defined in this manner should be avoided. Otherwise, issues that the lawyer thought were not part of the engagement may appear later, from the client's viewpoint, to be issues the lawyer negligently failed to raise.

© The Regents of the University of California

D. Defining the Fee

§1.19 1. The Fee Agreement

The initial interview is the best time for fixing the fee, or at least its terms and limits. See, *e.g.,* ABA Model Rules of Prof Cond 1.5(b). A frank discussion of the probable fee and the elements that go into it will help establish a good client relationship and may prevent future misunderstandings. The agreement should be flexible enough to allow for reasonable compensation if the lawyer renders additional services.

With some exceptions, the Business and Professions Code requires that fee agreements be in writing and include particular provisions. Bus & P C §§6147 (contingency fees), 6148 (noncontingent fees).

Failure to comply with the statute renders the fee agreements voidable at the client's option, and the lawyer may recover only a "reasonable fee," not the amount provided for in the noncomplying agreement. Bus & P C §§6147(b), 6148(c). Under §6148, a written contract for lawyers' services is required, with some exceptions, if it is reasonably foreseeable that the total cost to the client will exceed $1000. The statute discusses "total expense to the client," not merely attorney fees. Therefore, other fees or costs such as deposition expenses must be considered. The contract must show the hourly rate or the standard rates, fees, and charges applicable to the matter. The general nature of the legal services and the respective responsibilities of the lawyer and the client in pursuing the matter must also be set out. The State Bar of California has prepared sample contracts, which are available at a nominal charge by writing to the address in the Directory. See also Fee Agreement Forms Manual (2d ed Cal CEB 2007).

It is not enough merely to obtain the client's signature on a retainer agreement. See, *e.g.,* Cal Rules of Prof Cond 4-200, which permits consideration of the client's consent as a factor in determining the fee only if that consent is informed. See also *Mazuran v Stefanich* (1928) 95 CA 327, 272 P 772, in which the court noted that clients typically rely on the lawyer's draftsmanship, even for the fee agreement.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/1 Lawyer's Role in Real Property Sales/§1.20 2. Amount of Fee

§1.20 2. Amount of Fee

In arriving at the fee amount, it is proper to consider all the facts and circumstances of the engagement, including these factors (Cal Rules of Prof Cond 4-200):

- The amount of the fee in proportion to the value of the services performed;
- The relative sophistication of the lawyer and the client;
- The novelty and difficulty of the issues and the skill required;
- The likelihood, if not apparent to the client, that acceptance of this particular employment will preclude other employment for the lawyer;
- The amount at stake and the results obtained;
- The time limitations imposed by circumstances or the client;
- The nature and length of the lawyer's relationship with the client;
- The lawyer's experience, reputation, and ability;
- Whether the fee is fixed or contingent;
- The time and labor required; and
- The client's informed consent to the fee arrangement.

See also ABA Model Rules of Prof Cond 1.5(a), 1.5(c). The client's inability to pay or an unreasonable burden on the attorney may also be factors. ABA Model Rules of Prof Cond 6.1, 6.2(b).

Attorneys may wish to inform their clients of the tax effects of legal fees. Reasonable fees, if they are ordinary and necessary, are deductible if they fall within the Internal Revenue Code definitions of expenses for business (IRC §162); expenses for the production of income or for management, conservation, or maintenance of income-producing property (IRC §212(1)-(2)); or expenses in connection with the determination, collection, or refund of any tax (IRC §212(3)). Not deductible, however, are expenses paid or incurred in acquiring, defending, or perfecting title, recovering possession, or developing or improving property. These fees are capital expenditures and are added to the cost of the property. See, *e.g.,* Treas Reg §1.212-1(k).

However, before discussing tax effects, the lawyer should consider the specialist standards that are likely to apply to tax advice (see §1.14) and the scope of the lawyer's engagement (see §1.17). If tax advice is part of the engagement, then advice on the tax effects of the legal fees will be within the scope of the engagement. If tax advice is not part of the engagement, the lawyer should advise the client to consult with a tax specialist to advise the client on any tax issues relating to the transaction or the tax effect of legal fees.

© The Regents of the University of California

§1.21 3. Equity Interests

Sometimes a client suggests that the lawyer accept an equity interest in the transaction as the fee for performing necessary legal services. Even though the lawyer invests no money in the venture, an equity fee arrangement pits the lawyer's interest as a participant against the duty to have no interest adverse to the client. Practitioners are strongly advised to avoid such an arrangement, which creates a conflict of interest. This arrangement may be unenforceable, and the lawyer may be subject to discipline under Cal Rules of Prof Cond 3-300 or 3-310.

Equity compensation arrangements make it more difficult to revise the fee upward if additional services are required. Conversely, if the value of the lawyer's share greatly exceeds the lawyer's work, the client has paid more than a fair price for the legal services and the lawyer has charged what may be held to be an excessive fee. Cal Rules of Prof Cond 4-200; ABA Model Rules of Prof Cond 1.5(a), 1.5(c).

© The Regents of the University of California

III. IDENTIFYING CLIENT'S NEEDS AND OBJECTIVES

§1.22 A. Needs and Objectives as Important Guideposts

To provide effective legal services in a particular transaction, it is important to develop, through discussions with the client, a thorough understanding of the client's specific needs and objectives. At the outset, knowing the needs and objectives will help both lawyer and client determine the lawyer's role and the nature and scope of legal help required. As the transaction progresses, the lawyer can better identify issues that bear on these needs and objectives and fashion appropriate means to address them.

The nine discussion areas treated in §§1.23-1.57 should, at a minimum, provide a helpful starting point.

© The Regents of the University of California

B. Areas to be Explored With Client

§1.23 1. Client's Purpose in Selling or Buying the Property

What is the true purpose (or purposes) behind the client's desire to sell or buy the property in question? The lawyer must have a clear understanding of the purpose in order to know what issues and alternatives to consider and how to relate them to the client's goals. And the client must have a clear picture of purpose in order to make informed decisions on these issues and alternatives. In discussions with the client, the lawyer should review and ascertain the relative priorities of the key purposes, which may include the objectives discussed in §§1.24-1.25.

© The Regents of the University of California

§1.24 a. Seller's Objectives

The seller's objectives in a transaction may include one or more of the following:

- To lock in gains or losses;
- To convert an illiquid asset into liquid assets;
- If the property is investment property, to "trade" to another property that is larger, smaller, or otherwise more suitable;
- If the property is residential property, to "trade" to another residence in the area that is larger, smaller, or otherwise more suitable; or to sell because of, *e.g.,* a job transfer or changes in family circumstances;
- If the property is the site of the seller's business, to relocate the business to a more suitable site; and
- To raise cash to deal with other financial needs.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/1 Lawyer's Role in Real Property Sales/§1.25 b. Purchaser's Objectives

§1.25 b. Purchaser's Objectives

The purchaser's objectives in the transaction may include obtaining the property for one or more of the following:

- For the purchaser's own residential use;
- For the purchaser's own business use;
- For investment;
- For some combination of residential use, business use, and investment; and
- Because of certain features that are important to the purchaser (*e.g.,* the property adjoins property already owned by purchaser; its size, its location, or the availability of water or other utilities make the property especially suited to the purchaser's intended uses; or the property appears to be the most suitable property in the area to achieve the purchaser's need for a tax-deferred exchange).

© The Regents of the University of California

§1.26 2. Alternatives to Sale

As part of the process of identifying the client's purpose, review with the client any alternatives to sale or purchase that might apply to the client's circumstances. A review of alternatives will be helpful in two respects: First, it will bring appropriate alternatives to the client's attention early, when the client's ability to plan and decide is least constrained. Second, the process of considering the different risks and effects of these alternatives will help test and clarify the client's key objectives. Examples of alternatives are discussed in §§1.27-1.36.

© The Regents of the University of California

a. Seller's Alternatives

§1.27 (1) Leasing Transaction

A lease might be the most appropriate alternative in several circumstances:

- A lease rather than a sale of the property may be of interest to a seller who occupies the property now but does not need to continue to do so, needs some liquidity now, and would prefer to retain a long-term interest in the property.
- A lease of part of the property might be of interest to a seller who needs some liquidity, but also needs to continue to occupy at least some space on the property.
- A seller wanting liquidity but needing to continue to occupy the entire property might consider a sale-leaseback transaction.
- A seller considering a sale of the property in order to move elsewhere but concerned about the permanency of the move might consider leasing the property, at least for the period of uncertainty.
- A seller who wants liquidity and a retained interest in the property but is not interested in direct management of the property might want to consider a ground lease under which the actual leasing and management of the property would be done by the ground lessee.

Leases for terms of up to 99 years on town and city lots (CC §718), and up to 51 years for agricultural or horticultural purposes (CC §717), provide income, which is generally adjusted periodically for increases in rental values or the cost of living. A long-term lease usually provides that taxes, insurance, maintenance, and repairs are to be paid by the tenant, giving the landlord what amounts to an annuity for the leasehold term, the success of which depends on the tenant's ongoing financial ability to perform its obligations. At the end of the term, the landlord (or probably the landlord's heirs) regains possession of the property. If rent is not prepaid, a lease generates little *current* cash compared with a sale, and rent is taxable as ordinary income. On long-term leases generally, see Ground Lease Practice (2d ed Cal CEB 2009).

© The Regents of the University of California

§1.28 (2) Other Sources of Liquidity

If the seller's essential purpose is to gain liquidity, review with the seller any other potential sources of liquidity that may apply. Generally, the possibilities will fall into two broad categories, either debt sources (see §1.29) or equity sources (see §1.30).

© The Regents of the University of California

§1.29 (a) Debt Sources

One source of liquidity will be money raised by borrowings secured by the property. The key questions will be what amounts of money are realistically available for borrowing against the property, what the cost of such borrowing will be to the client, and whether such borrowing will address the seller's long-term needs or will instead provide some immediate relief but create new, perhaps more difficult, needs in the future.

On secured financing for commercial loans, see California Real Estate Finance Practice: Strategies and Forms (Cal CEB 2000).

© The Regents of the University of California

§1.30 (b) Equity Sources

Money may also be raised as equity. The ways this can be accomplished are many and varied. Most of them also involve costs, risks, and complexities that differ greatly from those of a straightforward sale (and are also beyond the scope of this chapter). The extent to which the lawyer will find it appropriate to review these alternatives with the client will depend not only on the client's purpose but also on the client's level of sophistication and tolerance for risk. Examples of possible equity alternatives:

- Sale of undivided cotenancy interests in the property;
- Syndication of the property (*i.e.,* forming a limited liability company or limited partnership to own the property and selling interests in the new entity);
- Subdividing or converting the property to condominiums and then selling individual parcels or condominium units (see §1.31).

© The Regents of the University of California

§1.31 (3) Development of the Property in Furtherance of Sale

The seller may wish to consider whether development of the property will facilitate a sale of the property. The appropriateness of development will depend largely on the client's purpose and level of sophistication, and whether the investment of time and money is likely to result in an increase in value substantial enough to justify the expense and risk of development. The following are examples of presale development activities that the seller may wish to evaluate:

- **Subdivision.** Subdividing the property, which may simply involve splitting the property into two or more pieces, or it may involve the creation of two or more lots, parcels, condominium units, or other divisions, pursuant to a more formal subdivision plan; exactly what is done, and how it is done, will vary according to circumstances, including such factors as whether the property initially is unimproved or is already partly or fully improved, and whether and to what extent the client wants (or will be required) to improve (or further improve) the property as part of the subdivision process and the rules of the local jurisdiction;
- **Condominium Conversion.** In the case of property improved with a building used or usable as a multi-tenant building, whether commercial or residential, converting the building into a commercial (or residential, as the case may be) condominium;
- **Improvement to Undeveloped Property.** In the case of undeveloped property, fully developing it or, alternatively, making basic infrastructure improvements.
- **Altering Existing Improvements.** In the case of already-developed property, replacing the existing improvements with new improvements, upgrading existing improvements, increasing the density of the improvements, or changing the nature of the improvements (*e.g.,* from low-rise industrial to mid-rise commercial).

© The Regents of the University of California

§1.32 (4) Other Sources of Relief

If the seller's essential purpose is to raise money to meet pressing financial needs, the lawyer should review the circumstances in detail with the seller so that the exact nature and extent of the seller's difficulties are clearly understood. Depending on the circumstances, it may be appropriate to consider a workout program with the seller's creditors (which may or may not include a sale of the property) or seek bankruptcy protection. If the lawyer is not an experienced bankruptcy practitioner, the lawyer should advise the client to consult with bankruptcy counsel who specialize in debtor representation.

© The Regents of the University of California

§1.33 b. Purchaser's Alternatives

The purchaser's alternatives are substantially the same as the seller's, except that they must be viewed from a different perspective. The purchaser's alternatives are discussed in §§1.34-1.36.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/1 Lawyer's Role in Real Property Sales/§1.34 (1) Leasing Transaction

§1.34 (1) Leasing Transaction

If the purchaser is interested in the property for the purchaser's own use, a lease of an initial term of 1 to 5 years (coupled with options to extend, expand, or both, as appropriate) may provide needed flexibility when, *e.g.,*

- the purchaser does not presently need the entire property, and future needs are uncertain;
- the purchaser needs the entire property now (or in the near future) but expects to outgrow the property in a period of years; or
- for any other reason, the purchaser is unsure of how long the size, type, or location of the property will remain suitable.

On leasing generally, see Retail Leasing: Drafting and Negotiating the Lease (Cal CEB 2007); Office Leasing: Drafting and Negotiating the Lease (Cal CEB 1996); and Ground Lease Practice (2d ed Cal CEB 2009).

© The Regents of the University of California

§1.35 (2) Other Equity Transactions

If the purchaser is interested in the property but would prefer to own only a part of it (or a shared interest in all of it), the purchaser might want to explore some of the alternatives discussed in §§1.27, 1.30-1.31, 1.34-1.35. The user of an office building or commercial space, for example, might want to explore a leasing transaction coupled with equity participation in the overall building project (or some variation involving shared ownership and shared occupancy). Similarly, a potential residential or commercial user who wants to own but has relatively modest space needs might be especially interested in a residential or commercial condominium project.

© The Regents of the University of California

§1.36 c. The "Go/No-Go" Alternative

The lawyer and the client also need to consider the alternative of not pursuing any transaction at all. This alternative should be considered in the initial interviews with the client, and it is an option worth reconsidering from time to time as transactional negotiations progress. It may become evident that the client really does not want to sell the property, and this knowledge can help the client avoid the mistake of completing a transaction it did not want or need to conclude. At minimum, this knowledge will influence the negotiation of the transaction. If the client does not need to sell the property or is ambivalent about a sale, the seller's negotiating position with the purchaser will be much stronger and this added leverage will be a key factor in the negotiation of the transaction.

© The Regents of the University of California

§1.37 3. Client's Timing Needs

Timing is often a crucial part of the client's overall needs and objectives that the lawyer needs to understand.

© The Regents of the University of California

§1.38 a. Ascertaining Client's Needs

The lawyer must first ascertain the client's needs by reviewing the following:

- Whether the client needs the sale to close by a particular time;
- In the case of a seller, whether the client needs to receive the net proceeds of sale by a particular time (this issue will bear not only on the time of closing but also on whether—and if so, in what amount, and for how long—the seller can consider taking back a secured note for part of the purchase price);
- Whether any financing secured by the real property is coming due and whether the client has the ability to renew or find new financing; and
- In the case of a purchaser, whether the client needs a particular amount of time in which to deal with the presale contingencies discussed in §1.70.

© The Regents of the University of California

§1.39 b. Degree and Causes of Any Timing Requirements

The lawyer should review the timing needs with the client and, if the needs are urgent, the particular circumstances causing the urgency. It is especially important to fully understand the *causes* of any timing urgency, because different causes can affect the client's approach to a transaction. For example, the timing may be driven by nontransaction-related needs, and fulfilling those needs may be more important to the client than price or cost; *i.e.,* the client may be prepared to accept an early offer—before fully testing the market—or accept more risk, or both, in order to achieve a quick sale or purchase.

© The Regents of the University of California

§1.40 (1) Seller Timing Requirements

Timing may be urgent for the seller when, *e.g.,* (1) the seller is in financial difficulty or needs to raise cash to fund the purchase of another property already in escrow or pay off the current financing on the property which is coming due; (2) when the seller must move elsewhere within a particular time and is not in a position to do so until the property is sold; or (3) if the property is part of seller's business operation, when it is important to the seller for financial accounting purposes to book the sale of the property (and/or a loss from discontinued operations conducted on the property prior to sale) within a particular financial period. Although the time pressure on the seller generally is to shorten the time to close (nourished, often, by the additional general concern that longer time periods increase the chances that the purchaser's ardor for the sale may cool), sometimes the seller needs more time. Examples include a seller who is moving and has not yet purchased or leased property in the new location, and a seller who intends a tax-deferred exchange and needs time to locate a suitable exchange property.

In other instances, timing may be directly linked to price. A common example is when the seller will incur significantly greater income tax cost if the sale is closed in a subsequent year rather than in the current year.

© The Regents of the University of California

§1.41 (2) Purchaser Timing Requirements

On the one hand, quick timing may be urgent for a purchaser who needs to occupy the property by a particular deadline. This situation might occur, *e.g.,* in the following cases:

- The purchaser is obligated to vacate the property it now occupies by that date;
- The purchaser's present property is too small and the purchaser's need for the additional room provided by the new property is urgent;
- The purchaser intends to make improvements that are essential to the expansion of the purchaser's business and will lose a market window if the improvements are delayed beyond a particular date; or
- It is necessary to complete this purchase in order to complete a tax-deferred exchange or to accommodate specific tax or financial accounting objectives.

On the other hand, deferred timing may be urgent when, *e.g.,* the purchaser must have time to sell other property to fund this purchase or to satisfy contingencies relating to the condition of the property or to the feasibility of the purchaser's planned use of the property.

© The Regents of the University of California

§1.42 4. Net Proceeds Requirements

The lawyer and client should ascertain the net result the client needs to achieve from the sale. Determine the absolute bottom line (see §1.43) and distinguish between the client's needs and the client's wants (see §§1.44-1.46).

© The Regents of the University of California

§1.43 a. The Bottom Line

It is vital to focus on the ultimate net results to the client. The factors of price, selling expenses, closing costs, income tax costs, and the costs of legal, accounting, and other expert services engaged by the client to assist in the transaction must obviously be considered. But other factors that might not initially be as obvious should also be considered, such as:

- The carrying costs of the property during periods of marketing and escrow;
- The cost to the seller of any continuing responsibilities for the property assumed by the seller under the sale agreement (and the cost to the purchaser of responsibilities not so assumed by the seller);
- The potential costs of contingent liabilities arising from any seller warranties or indemnification obligations that survive the closing of the sale (and the potential costs to the purchaser for items that do not survive closing);
- The increase in property taxes resulting from reassessment of the property after the sale;
- The cost of sales taxes if personal property subject to such tax is included in the transaction;
- The cost of any local transit tax or other special taxes that may be triggered by the purchaser's new occupancy, or installation of improvements for occupancy, of the property;
- The effect of inflation if lengthy time periods are involved; and
- The effect of changes in currency exchange rates if foreign currencies are involved.

© The Regents of the University of California

§1.44 b. Distinguishing Between Wants and Needs

What the client wants and what the client needs may be two different things. The lawyer must ascertain where the client stands on both points and must also help the client place them in a workable perspective.

© The Regents of the University of California

§1.45 (1) Wants

Ascertaining the client's wants may not be easy. Sometimes a client will arrive at the lawyer's office with a definite deal in mind that will be unalterable throughout the transaction. More often, the client will be unsure, especially if there are no pressing needs. Perhaps the most difficult situation is when the client is determined to get "top dollar" for the property (in the case of a seller) or to give "bottom dollar" for the property (in the case of a purchaser), but has no clear sense of what that amount might be or how one goes about getting it. Such a client is not likely to be happy until he or she can develop (and become comfortable with) an understanding that the value of property at any particular time is a function of what a buyer, available, willing, and able at that time, is prepared to pay for it. It may be helpful in this situation to review in detail with the client the various techniques, discussed in §§1.104-1.113, for marketing the property.

© The Regents of the University of California

§1.46 (2) Needs

When urgent needs exist, they may substantially influence both the client's wants and the deal itself. For example, if the seller's key purpose of the sale is to pay certain debts or to fund another purchase, the nature and amount of the financial need may establish a floor for what the client must net from the sale. In an extreme case, the need may even dictate whether the sale makes sense at all. For instance, if a client with financial troubles must realize an amount that exceeds the likely market value of the property, it may well be that the client should be focusing on either additional or alternative ways to resolve those troubles.

Further, the lawyer should be familiar with the terms of any loans secured by the real estate. There may be limits on the seller's ability to pay off the loan, and in a down market, the loan could be worth more than the real estate (known as being "underwater"), giving the lender a strong voice in any the terms of any proposed transaction.

In a purchaser's case, the purchaser's financial condition or other needs that are competing for the purchaser's available financial resources may set definite limits on both the overall cost that the purchaser can afford to incur and the manner in which that cost will be funded.

© The Regents of the University of California

§1.47 5. Client's Risk Tolerance: Presale Contingencies

The lawyer should review with the client the various presale contingencies that a prospective purchaser of the property may want to include in the sale agreement. Whether presale contingencies will be accepted by a seller at all will depend on whether there is a "buyer's market" and the buyer has the superior bargaining position. If that is the case, a seller is more likely to agree to more presale contingencies benefiting the purchaser. Some typical contingencies are discussed in §1.70. The lawyer should also determine the extent to which the client will be in a position to accommodate such contingencies, which will enable the lawyer to assess such contingencies and also develop strategies for dealing with them. The possibilities cover wide spectrums for both the seller and the purchaser.

© The Regents of the University of California

§1.48 a. Seller's Presale Risk Tolerance

At one extreme, the seller may have high presale risk tolerance (or may have limited bargaining leverage, particularly in a falling market or if a property is "underwater," *i.e.,* the seller owes more on the real estate loan secured by the property than the property is worth), in which case the strategy may be to accept broader contingencies and longer contingency periods in order to obtain a higher price. As the seller's tolerance decreases, the strategy will be to narrow the number and scope of contingencies and shorten contingency periods. At the other extreme, the seller may have no presale risk tolerance (or may have the superior bargaining leverage). In that case, the strategy will be to insist that the prospective purchaser conduct its studies and inspections without execution of an agreement (other than an agreement, if appropriate, covering the inspections themselves) and to make the sale agreement, if an agreement is ultimately reached, a closing document. Alternatively, the parties may enter into a purchase and sale agreement that has no specific purchaser contingencies but only a very short due diligence period within which the purchaser must complete all of its due diligence investigations and inspections and, at the end of the period, decide whether to terminate the agreement or close the transaction.

© The Regents of the University of California

§1.49 b. Purchaser's Presale Risk Tolerance

The strategies of the purchaser are much the same as those of the seller: A confident purchaser with high presale risk tolerance may see an opportunity to obtain a better price by offering few contingencies and short time periods. In a down real estate market, there may be opportunities for a purchaser with a higher risk tolerance to acquire property at a "discount" by bidding at a foreclosure sale, purchasing property in default from a foreclosing lender, or purchasing "REO" (real estate owned) property acquired by a lender from a defaulting borrower. However, in such circumstances, the purchaser may have limited opportunity to conduct due diligence with respect to the property and, if purchasing property directly from a lender, may receive no or limited representations concerning the property. On REO property, see §§6.110-6.111.

If a purchaser needs to finance its acquisition, not only should the purchaser determine its own risk tolerance, but also that of its proposed lender. Depending on the current lending climate, a purchaser may be willing to take greater risks regarding certain contingencies or be on a faster time line than its lender.

As the purchaser's risk tolerance decreases, the need for more time to satisfy broader contingencies increases. A purchaser with very low presale risk tolerance may wish to consider an option agreement that may cost the purchaser some option money but will keep open for the duration of the option period the purchaser's complete freedom to decide whether to go through with the purchase. On options, see chap 8.

© The Regents of the University of California

§1.50 6. Client's Risk Tolerance: Postsale Contingencies

The lawyer should review with the client the various contingencies that may result in cost or liability to the client after closing and determine the extent to which the client is in a position to assume the risk of those contingencies. Some examples are discussed in §§1.51-1.53.

© The Regents of the University of California

§1.51 a. Seller Financing

The lawyer should review whether and to what extent the seller is in a position to provide part or all of the purchase financing. The risks discussed with the seller should include the purchaser's financial ability; the risks of enforcement, including time, expense, and the effects of the one-form-of-action and antideficiency provisions of CCP §§580b, 580d, and 726; the effect of senior liens, if the seller's carryback deed of trust is not in first position; and the effect of a purchaser bankruptcy. Seller financing can increase the attractiveness of the property to a buyer in a weak market.

See chap 9 on seller financing.

© The Regents of the University of California

§1.52 b. Condition of Property

The lawyer should review whether and to what extent the client is in a position to assume responsibility for the cost of correcting defects or other deficiencies discovered after closing with respect to the condition of the property. The seller's ability to avoid risk will, of course, be subject to some limitations imposed by law; the attorney should review these limitations thoroughly with the client. Such limitations include the law of fraud, the law of mistake, and the potential responsibility for hazardous waste remediation under environmental laws. Even with these limitations, however, a broad area of risk remains that the seller and the purchaser are free to allocate to one or the other (or to both on a shared basis) in the sale agreement. See §§4.95-4.97, 4.107.

See §§7.61-7.72 on indemnification and the use of release clauses in the context of hazardous waste liability.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/1 Lawyer's Role in Real Property Sales/§1.53 c. Other Postsale Problems

§1.53 c. Other Postsale Problems

The lawyer should review whether and to what extent the client is in a position to assume responsibility for other problems discovered after closing. Examples include:

- For property currently producing income, disappointing postclosing operating results; and
- For undeveloped property (or property whose use is to be materially changed), disappointing postclosing results of the development (or change of use) attempted by the purchaser.

© The Regents of the University of California

§1.54 7. Client's Tax and Financial Accounting Requirements

A sale and purchase of the property will have both tax and financial accounting consequences to both the seller and the purchaser. Both lawyer and client need to clearly understand what those consequences will be. In addition, the lawyer must know whether there are particular tax or accounting objectives that the client wants or needs to achieve. These objectives may be affected by the timing of the transaction (as discussed in §§1.39-1.41), by the structure of the transaction (*e.g.,* as a nontaxable exchange rather than a taxable sale), by allocations made as part of the transaction (*e.g.,* allocations of price as between land and depreciated/depreciable improvements), or by other aspects of the transaction (*e.g.,* significant postsale risks assumed by the seller may, depending on the circumstances, need to be disclosed as contingent liabilities in the seller's financial statements or other documents disclosing information about the seller's financial condition). If the lawyer is not a tax specialist, the client should be advised to consult with a tax specialist about the tax implications of the transaction.

Recognized gain from a taxable disposition of real property that constitutes a capital asset or IRC §1231 property held can differ depending on the characterization of the gain for federal income tax purposes. Recognized gain from the disposition of dealer property or real property not held for more than 1 year is taxed at ordinary income rates.

© The Regents of the University of California

8. Client's Knowledge and Experience Concerning the Property

§1.55 a. Seller's Knowledge and Experience

The lawyer should review with the seller the duration of the seller's ownership of the property and the extent of the seller's information about the property. This review will be important in ascertaining the nature and extent of the disclosures the seller will be in a position to make about the property. It will also be important in assessing whether and to what extent further investigations by the seller will be needed or appropriate. The kinds of investigations that may be involved are discussed more fully in §§1.59-1.69.

© The Regents of the University of California

§1.56 b. Purchaser's Knowledge and Experience

The purchaser may be a complete stranger to the property or may already have a fair amount of information about it. Examples of the latter situation are a purchaser who is currently a tenant on the property, a purchaser who owns adjoining property, and even a former owner of the property desiring to have it back again. Familiarity with the property will not lessen the purchaser's need to investigate with care, but it may affect the nature and scope of the investigations that will be needed. Usually, prior knowledge of the property will help sharpen the focus of the purchaser's investigations, thereby increasing both the efficiency and the effectiveness of the effort. On purchaser's investigations, see §§1.70-1.93.

© The Regents of the University of California

§1.57 9. Client's Transactional Resources

The lawyer should review with the client the nature and extent of resources already available to the client to assist in selling or purchasing the property. Depending on the nature and scope of the transaction, the client may need expert assistance—in addition to the lawyer's help—from any one or more of a variety of other experts, including accountants, bankers, mortgage brokers, title and escrow officers, appraisers, real property brokers, real estate investment consultants, surveyors, structural engineers, insurance brokers, soils engineers, hydrologists, environmental consultants, architects, contractors, and land use and other political consultants. The client may have internal expert resources and existing relationships with outside experts who can fill many of these needs. The lawyer will need to know who those experts are and in what areas they will be assisting. The lawyer also will need to ascertain whether there are any outside experts the client will require assistance in engaging.

In assisting the client, the lawyer should be aware that many specialist areas are regulated by the state and that practitioners in such regulated fields are not permitted to claim to be specialists unless they have met the state's standards and have been properly licensed. For example, the U.S. Environmental Protection Agency's "all appropriate inquiries" rule, which took effect November 1, 2006, requires that, incident to a prospective purchaser's duty to discover the environmental risks relative to the purchase of real property, all Phase I environmental site assessments must be conducted by or under the direct supervision of a qualified environmental professional and establishes specific education and experience requirements for an environmental consultant. 40 CFR §312.10(b). The lawyer should also remember that there is no authority inherently implied in the lawyer-client relationship to engage assistants at the client's expense. *Cormac v Murphy* (1922) 58 CA 366, 208 P 360. If the lawyer concludes that the client needs assistance from additional experts, the lawyer must be sure that the client agrees to the engagement and is prepared to bear the expense. The lawyer should also consider whether particular experts should be retained by the lawyer (if it is appropriate in the circumstances to protect reports and other work produced by the expert as part of the lawyer's work product) or directly by the client.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/1 Lawyer's Role in Real Property Sales/§1.58 IV. PRECONTRACT DUE DILIGENCE

§1.58 IV. PRECONTRACT DUE DILIGENCE

Before the property is put on the market for sale, the seller should assemble and review information about the property. This due diligence review will enable the seller to identify potential issues that will affect the marketing, pricing, and negotiation of the purchase agreement. Similarly, the purchaser may find it useful to conduct some preliminary due diligence and planning before the purchase agreement is signed, because the information acquired may affect negotiation of the purchase agreement.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/1 Lawyer's Role in Real Property Sales/ A. Precontract Due Diligence Matters to Review With Seller/§1.59 1. Seller's Objectives

A. Precontract Due Diligence Matters to Review With Seller

§1.59 1. Seller's Objectives

From the seller's standpoint, the objectives of precontract due diligence are the following:

- To determine (assuming the seller has a choice) whether the present time and circumstances are suitable for attempting to sell the property;
- To eliminate any problems with the property that are better addressed before the property is put on the market;
- To comply with any applicable disclosure requirements imposed by federal and state statutes or local ordinances and common law, such as the Natural Hazard Disclosure Statement (CC §§1103-1103.14; see §6.50); commercial earthquake safety disclosures (see §§5.16-5.17); and, after January 1, 2010, certain energy consumption disclosures about nonresidential buildings to a prospective purchaser, a lessee of the entire building, and a lender financing the entire building (Pub Res C §25402.10);
- CC §§1102-1103.14 (residential sales disclosures);
- CC §1102.6b (property subject to Mello-Roos Community Facilities Act (Govt C §§53311-53368.3) lien or a fixed lien assessment securing bonds issued under the Improvement Bond Act of 1915) (Str & H C §§8500-8887) or to a contractual assessment program authorized by CC §§5895.10-5898.32;
- CC §1102.6c (note that California property tax law requires assessor to revalue real property at time of change of ownership, which may result in receipt of supplemental property tax bill);
- CC §§1103-1103.14; Govt C §§8589.3-8589.5, 51183.5 (location of property in special flood hazard area, area of potential flooding, very high fire hazard severity zone, wildland fire area, earthquake fault zone, or seismic hazard zone);
- CC §1102.15 (ordnance location within one mile of property);
- CC §1102.16 (window security bars and any safety release mechanism on those windows);
- CC §1102.17 (adjacent property affected by or zoned for industrial use; see §6.46);
- CC §1368 (common interest developments);
- CC §§2079.7 (environmental hazards), 2079.8 (residential geologic and seismic hazards), 2079.9 (commercial seismic safety), and 2079.10 (energy rating program);
- Govt C §§8875.6-8875.95 (seismic information on certain unreinforced masonry buildings);
- Govt C §§8897.1-8897.2 (residential sales seismic disclosures);
- Health & S C §13113.8 (smoke detectors);
- Health & S C §13113.9 (burglar bars on residential dwellings);
- Health & S C §25359.7 (hazardous substances; see §1.64);
- Pub Res C §2621.9 (earthquake fault zones);
- Pub Res C §2694 (seismic hazard zone);
- Pub Res C §4136 (property in forest fire risk area); and
- Local ordinances covering such matters as energy conservation, termite control, and building permit status (see chaps 4, 6); and
- To anticipate other problems that will need to be disclosed and can best be raised at the beginning of negotiations, when discussion of the problems will do the least harm to the seller's negotiating position in the deal. Presale issues to be reviewed with the seller include the issues discussed in §§1.60-1.69.

In the wake of the terrorist attacks of September 11, 2001, the federal government promulgated the following restrictions:

- Executive Order No. 13224 (Sept. 23, 2001) prohibits "any transaction or dealing by United States persons or within the United States in property or interests in property" of suspected terrorists and persons or organizations associated with suspected terrorists. Both sellers and purchasers should check the U.S. Department of Treasury,

Office of Foreign Assets Control, list of "specially designated nationals and blocked persons." For further information, see http://www.treas.gov/offices/enforcement/ofac; and

- Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (USA Patriot Act) (Pub L 107-56, 115 Stat 272) imposes certain restrictions and reporting requirements on financial transactions to prevent, detect, and prosecute international money laundering and the financing of terrorism.

© The Regents of the University of California

§1.60 2. Consider Valuation of Property

If the client has retained a real estate broker, the broker should provide market information to assist the client in determining the value of the property and a proposed purchase price for marketing purposes. If there is no real estate broker involved, the lawyer and client should discuss whether there is a need to obtain an appraisal or other expert information on the value of the property. This need can arise in various contexts. The information may simply be needed to provide market information needed to establish a proposed asking price for the property or a formal valuation may be imposed by law (*e.g.,* a court-supervised sale in which the sale price must be within a certain percentage of the property's appraised value) or by contract (*e.g.,* a sale made under a cotenancy agreement or a right of first refusal, requiring that the price be based on the property's appraised value). The more rapidly moving a market is, whether up or down in price, the more difficult it is to determine the value of the property.

© The Regents of the University of California

§1.61 3. Review Condition of Title

Obtain (or have the client obtain) from a title company and review a current preliminary report on the condition of title to the property and copies of all easements, deeds of trust, and other exceptions shown in the preliminary report. If any title exceptions could create a problem, consider whether to work at removing them before the seller is committed to a sale. See §§4.53-4.57.

If there is an existing loan secured by the property, the lawyer should review the loan documents to ascertain the following:

- Can the loan be assumed by a new purchaser and, if so, under what terms and conditions?
- Can the loan be paid off before the maturity date? If so, is there a prepayment penalty? Other conditions?
- Is there a "lock in" clause that prohibits a prepayment before the maturity date?

Many securitized loans prohibit prepayment of the loan, but allow for a defeasance of the loan. Defeasance involves substituting government-backed securities as collateral for the loan and a release of the real property security to permit a sale of the real property. If there will be a defeasance, the lawyer should contact the lender immediately to discuss the lender's defeasance requirements, because that process will require additional time and cost that the seller and lawyer will need to take into account when negotiating the terms of the purchase agreement.

For discussion of the role of the lawyer in title insurance matters, see California Title Insurance Practice §§2.4-2.35 (2d ed Cal CEB 1997). On preliminary reports, see Title Ins, chap 5.

© The Regents of the University of California

4. Review Condition of Property

§1.62 a. Existing Information

The lawyer should assist the seller in marshaling all information currently available to the seller on the condition of the property. In this connection, identify any physical problems with the land or improvements that might be better corrected before the sale.

© The Regents of the University of California

§1.63 b. Additional Information

The lawyer should review with the seller any other investigations that it may be prudent to conduct before the property is placed on the market. The information gathered (see §1.62) may reveal conditions that should be clarified by further investigation or reveal issues that may affect negotiations.

If there are existing leases, are any of the leases expiring soon? Are any of the tenants in default? Does the seller, as landlord, have significant obligations to any tenants, such as the obligation to build out tenant improvements or pay a tenant improvement allowance?

Many purchasers and their lenders will require that the seller deliver (as conditions to closing of the transaction) tenant estoppel certificates and subordination agreements. Do the leases require tenants to provide estoppels and subordination agreements? Within what time period? Is there a prescribed form of estoppel or subordination agreement that must be used?

If the property is undeveloped but the seller has obtained land use entitlements, when do those entitlements expire? Is the property subject to a development agreement with a governmental agency?

All of the above information will be relevant to contract negotiations.

© The Regents of the University of California

§1.64 c. Special Situation: Environmental Conditions

The lawyer should review with the seller both the state of the seller's existing information about the environmental condition of the property and the considerations involved in deciding whether more information is needed.

It should be considered a given that the seller will disclose to the purchaser any known contamination on the property. A statute covers part of the issue: The seller of nonresidential property who knows, or has reasonable cause to believe, that any hazardous substance is on or beneath that property must give the purchaser written notice of that condition. Health & S C §25359.7(a). In view of the likely materiality of this information to the purchaser, the entire issue, whether or not addressed in §25359.7, is probably covered by the principles of fraud or negligent misrepresentation. See also chap 7 on disclosure requirements concerning hazardous wastes and §6.53 on disclosure requirements concerning toxic molds.

A more difficult question for the seller is whether, and to what extent, to pursue information beyond that which the seller already knows. Generally, a seller is not required to inspect the environmental or other condition of a property and disclose the results of such inspection to the purchaser. Contrary to what may be the seller's initial instinct, however, it often makes good sense to further investigate the presence or absence of contaminants and the compliance of the property generally with environmental laws. There are two principle reasons for doing so:

- Additional information should help clarify the nature and extent of any problem (or help confirm the absence of a problem). If contamination is found, the seller may prefer to address the problem before marketing the property. Furthermore, whether or not contamination exists, the information should provide more exact data that will enhance both the quality of the seller's disclosures and the seller's ability to deal with the issues about the environmental condition of the property, which a purchaser will surely raise in the purchase transaction.
- Whether or not contamination is found, further information should help establish a "base line" concerning the present condition of the property, which could be useful to the seller after the property is sold.

See also §§6.47-6.50 on the seller's inspection of property for hazardous substances.

If an environmental audit is conducted, the lawyer should consider engaging an environmental consultant directly to provide a basis for protecting the audit results as lawyer-client privileged information. If the property is contaminated, the privilege may be important to preserving the client's rights in connection with any governmental or private action regarding the contamination. If the property is sold, of course, the privilege ceases to be important, because the seller will have disclosed the results of the investigation to the purchaser.

See chap 6 for a detailed discussion of environmental issues and approaches to addressing these issues in a purchase and sale transaction. See chap 4 for a detailed discussion of disclosures required for residential property. See also *Environmental Due Diligence: A Guide to Liability Risk Management in Commercial Real Estate Transactions*, 42 Real Prop. Prob. & Tr. J. 443 (2007-2008); *Representing Buyers, Sellers, and Lenders in Transferring Contaminated Property: A Primer for Real Estate Practitioners, Part I*, 35 Real Prop. Prob. & Tr. J. 305 (2000-2001); *Representing Buyers, Sellers, and Lenders in Transferring Contaminated Property: A Primer for Real Estate Practitioners, Part II*, 36 Real Prop. Prob. & Tr. J. 37 (2001-2002).

© The Regents of the University of California

§1.65 5. Review Legal Issues Affecting Property

The lawyer should review any legal issues that might be easier to correct before the outside world becomes aware that the property is to be sold, *e.g.*,

- The need for an easement (*e.g.,* for water line, access to public roads);
- The need to resolve potential easement claims by others;
- The need to resolve problems or disputes with an existing tenant or to negotiate a lease renewal or new rental rate;
- The need for a reciprocal parking agreement; and
- The need to address an encroachment problem with neighboring property.

For further discussion of legal title issues that should be addressed by the seller early in the sales process, see California Title Insurance Practice §§2.9-2.12 (2d ed Cal CEB 1997).

© The Regents of the University of California

6. Ascertain Whether Consents Needed From Others

§1.66 a. Internal Approvals

The lawyer should review any issues on internal approvals that the seller will need and ascertain whether any co-owners of the property will need to join in the sale. If the seller is an entity, the lawyer should learn what consents of, *e.g.,* members, partners, shareholders, or directors will be needed; what lead times will be required; and whether problems may arise in obtaining the consents. For form consents, see App D (corporation), and App E (limited liability company). On partnerships, see Statement of Partnership Authority, App F.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/1 Lawyer's Role in Real Property Sales/§1.67 b. External Approvals and Nonobjections

§1.67 b. External Approvals and Nonobjections

The lawyer should review any issues on obtaining external approvals, *e.g.,* liquor licenses (Department of Alcoholic Beverage Control), radio and television licenses (Federal Communications Commission), approvals under the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (15 USC §18a; 16 CFR §§801.1-803.90), or other governmental approvals or nonobjections; court approvals; approvals from the current lender; consent or waiver by the holder of an option or a right of first refusal; or other approvals or waivers required by material agreements to which the seller is a party.

© The Regents of the University of California

§1.68 7. Review Matter From Purchaser's Perspective

In advising sellers, the author has found it helpful to review with the seller the various matters that are likely to be on a prospective purchaser's due diligence list. The lawyer should therefore consider reviewing with the client the matters discussed in §1.70. This exercise may bring to mind additional items that the seller may wish to consider before placing the property on the market.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/1 Lawyer's Role in Real Property Sales/§1.69 8. Assist in Engaging Outside Experts

§1.69 8. Assist in Engaging Outside Experts

If the seller will retain outside experts, the lawyer should assist the seller as needed to be sure the terms of engagement are in writing and clearly define

- the nature and scope of work to be done; and
- the rate and basis of compensation to be paid.

PRACTICE TIP: The lawyer should also watch for the unduly restrictive liability limitations and overly protective indemnity provisions found in the form contracts of many consultants.

© The Regents of the University of California

B. Precontract Due Diligence Matters to Review With Purchaser

§1.70 1. Purchaser's Objectives

From the purchaser's standpoint, the objectives of precontract due diligence are to:

- Make an initial determination of the overall suitability of the property for the purchaser's intended needs;
- Identify presale contingencies that the purchaser will want to provide for in the letter of intent and the purchase agreement; and
- Identify any problems that need to be addressed (by elimination before closing, by price adjustment at closing, or by contractual provisions to be performed after closing).

Prepurchase issues to be reviewed with the purchaser are discussed in §§1.71-1.93; see also chap 4.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/1 Lawyer's Role in Real Property Sales/§1.71 2. Financing the Purchase

§1.71 2. Financing the Purchase

The lawyer should review with the client any financing from outside sources that the purchaser will need to acquire the property and to accomplish whatever development or other use the purchaser intends to make of the property. Include consideration of the following:

- The amounts needed for all phases of the project;
- The time or times at which various amounts of funding will be needed;
- The likely sources of such funding, which may include the seller, direct borrowing from a third party lender or lenders, indirect third party borrowing through assumption of assumable existing loans secured by the property, equity investors, or proceeds from the sale of other property owned by the purchaser;
- The likely availability of adequate funding from such sources;
- The estimated lead time needed to obtain a commitment for financing and to close the financing portion of the transaction, because this window period will be an essential element of the purchase agreement; and
- The due diligence and underwriting requirements of the lender; thus, if the lender will, for example, require a survey of the property, a Phase I environmental site assessment, a roof inspection report, or estoppel certificates and subordination agreements from the tenants, the purchaser will want to make sure these matters are covered in the purchase agreement.

© The Regents of the University of California

3. Legal Feasibility of Intended Use

§1.72 a. Necessary Approvals

The lawyer should review the issues and any local, regional, state, or federal agencies that are likely to be involved in obtaining, *e.g.,* development approvals, variances, and permits.

© The Regents of the University of California

§1.73 b. Effect of Applicable Laws

The lawyer should review the status and effect of local, regional, state, and federal laws that will bear on the purchaser's intended use and development of the property. Examples of such laws are set forth in §§1.74-1.90.

© The Regents of the University of California

§1.74 (1) Local and Regional Laws

Numerous local and regional laws need to be considered in evaluating the property to be acquired, including the impact of the following:

- General plans (see §1.75);
- Specific plans (see §1.76);
- Zoning ordinances (see §1.77);
- Building codes (see §1.78); and
- Subdivision approvals (see §1.79).

For a broad, but not exhaustive, list of additional local and regional laws to be considered, see §1.80.

© The Regents of the University of California

§1.75 (a) General Plans

Each local jurisdiction must have a general plan adopted under Govt C §§65300-65403, 65700. The plan's provisions may significantly affect how the property can be used. The general plan must include elements of land use; circulation; housing; conservation; open space; noise; safety relating to risks from seismic activity; slope instability, subsidence, and other geologic hazards; flooding; wildland and urban fires; growth of military readiness activities; and scenic aspects. Govt C §65302. The plan may also include any other elements that, in the judgment of the legislative body, relate to the physical development of the county or city. Govt C §65303. These elements may include, *e.g.,* recreation, transportation, transit, public services and facilities, public building, community design, redevelopment, and historical preservation.

© The Regents of the University of California

§1.76 (b) Specific Plans

Jurisdictions may also have specific plans that have been adopted to implement the general plan. Govt C §§65450-65457. Local approval of a proposed subdivision, construction project, or private sale of subdivided lots may be enjoined for inconsistency with the specific or general plan. Govt C §§66473.5, 66474; *Save El Toro Ass'n v Days* (1977) 74 CA3d 64, 141 CR 282; *Woodland Hills Residents Ass'n v City Council* (1975) 44 CA3d 825, 118 CR 856. Injunctive relief is also proper when a proposed public works project is inconsistent with the general plan. *Friends of "B" Street v City of Hayward* (1980) 106 CA3d 988, 165 CR 514.

© The Regents of the University of California

§1.77 (c) Zoning Ordinances

Local jurisdictions are empowered to enact zoning ordinances regulating land use in their territory by Cal Const art XI, §7, and Govt C §§65800-65918. The zoning ordinances of the jurisdiction in which real property proposed to be sold is located will substantially affect how the property can be used, and the lawyer must have a working knowledge of the local ordinances and the procedures to follow in obtaining zone changes, variances, and conditional use permits. For detailed discussion of zoning, see California Land Use Practice, chaps 4-5 (Cal CEB 2006). For a discussion on making a sale subject to specific zoning, see §4.86.

© The Regents of the University of California

§1.78 (d) Building Codes

The parties and their lawyers need to be aware of problems that may arise if an existing structure on the property does not comply with local building codes. Most local jurisdictions have adopted, with varying degrees of amendment and addition, the Uniform Building Code. The parties should check local codes as well as the records of the local building department concerning the property.

NOTE: A number of local jurisdictions have adopted or are considering adoption of green building standards and requirements. California has adopted the Green Building Standards Code as Part 11 of Title 24 of the California Code of Regulations. On green building, see California Construction Contracts, Defects, and Litigation, chap 4 (Cal CEB 2008).

The parties may wish to condition the purchase on compliance with local building ordinances. For discussion of making a sale subject to specific building codes, see §§4.87-4.89. On building codes, see California Land Use Practice, chap 11 (Cal CEB 2006).

© The Regents of the University of California

§1.79 (e) Subdivision Approvals

The lawyer needs to be aware of local requirements for subdivision approvals, because failure to comply with the Subdivision Map Act (see §1.83) and any local ordinances enacted under it will result in disapproval of the subdivision. Govt C §66473. See *Anthony v Snyder* (2004) 116 CA4th 643, 10 CR3d 505. Approval is precluded unless the local agency finds that the subdivision is consistent with the general plan and any applicable specific plans. Govt C §66473.5; See *Muzzy Ranch Co. v Solano County Airport Land Use Comm'n* (2008) 164 CA4th 1, 78 CR3d 691. In addition, if a lot split is not authorized, the local building department cannot issue a building permit or other required approval for development of the property. Govt C §66499.34; see *Wells Fargo Bank v Town of Woodside* (1983) 33 C3d 379, 189 CR 41. For discussion of Subdivision Map Act requirements, see California Subdivision Map Act and the Development Process (2d ed Cal CEB 2001).

© The Regents of the University of California

§1.80 (f) Miscellaneous Applicable Laws

The lawyer should be aware of the following:

- Applicable moratorium, or similar limitation on, *e.g.,* development, construction, timber removal, or issuance of water or sewer permits;
- Applicable rent control laws (see California Landlord-Tenant Practice, chap 7 (2d ed Cal CEB 1997));
- Applicable nuclear-free-zone legislation;
- Applicable historical landmark laws;
- Other laws relating to the condition of the property (see §§1.62-1.64; see also §§4.77-4.82);
- Local laws requiring receipt of a conditional use permit if there is a change in use of the property; and
- Local laws regulating the location of timber operations (but see *Big Creek Lumber Co. v County of Santa Cruz* (2006) 38 C4th 1139, 45 CR3d 21, holding that county ordinances restricting permissible locations for timber harvesting operations to specified zones were not preempted by state forestry laws, including the Z'berg-Nejedly Forest Practice Act of 1973 (Pub Res C §§4511-4517) and the California Timberland Productivity Act of 1982 (Govt C §§51100-51119.5)).

© The Regents of the University of California

§1.81 (2) State Laws

State laws that may affect the purchaser's decisions relating to acquisition of the property include the following:

- Environmental laws (see §1.82);
- The Subdivision Map Act (see §1.83);
- Vested rights decisions (see §1.84); and
- Laws regulating foreign investment and disposition of real property (see §1.85).

In addition, several other state laws need to be considered. See §1.86.

© The Regents of the University of California

§1.82 (a) Environmental Laws

A purchaser who intends to develop the property in a manner that will require a government permit or government approval needs to be aware of the California Environmental Quality Act (CEQA) (Pub Res C §§21000-21177), which, among other things, requires preparation of an environmental impact report for any project requiring government approval that may have a significant effect on the environment (Pub Res C §21100). Regulations on enforcement of CEQA are published in 14 Cal Code Regs §§15000-15387. On environmental impact reports, see §4.97. For full discussion of the environmental review process under CEQA, see Practice Under the California Environmental Quality Act (2d ed Cal CEB 2008).

Regardless of the purchaser's plans for the property, the purchaser must consider the effect of laws providing for the investigation and remediation of environmental contamination and for restrictions on use of property that is contaminated or is located in a contamination area. Such laws include the following:

- California's "superfund" law, the Carpenter-Presley-Tanner Hazardous Substance Account Act (Health & S C §§25300-25395.32);
- The Porter-Cologne Water Quality Control Act (Wat C §§13000-14076);
- The Hazardous Waste Control Law (Health & S C §§25100-25257.1);
- The Air Resources Law (Health & S C §§39000-44474);
- Laws relating to air pollution control districts (Health & S C §§40000-41357);
- Several other statutes collected in Division 20 of the Health and Safety Code; and
- The U.S. Environmental Protection Agency's standards and procedures for "all appropriate inquiries" (40 CFR pt 312; see also §1.57).

If there are environmental issues affecting the property, the purchaser should also investigate whether environmental insurance is available. See Nanney & Falbo, *Negotiation of Environmental Insurance*: *Policy Clarifications That Insurers May Give,* 26 Cal Real Prop J 30 (Winter 2008). For more detailed discussion, see chap 7.

© The Regents of the University of California

§1.83 (b) Subdivision Map Act

If the property to be sold is part of a larger parcel or if the purchaser intends to divide the property after the sale, the lawyers for both parties must be aware that the Subdivision Map Act (Govt C §§66410-66499.37) gives each local governing entity jurisdiction over subdivisions in its area (Govt C §66411; see *Kalway v City of Berkeley* (2007) 151 CA4th 827, 60 CR3d 477) and establishes an approval procedure that must be followed whenever land is subdivided (Govt C §§66451-66472.1; see, *e.g., Anthony v Snyder* (2004) 116 CA4th 643, 10 CR3d 505). As defined in Govt C §66424, subdivision

> means the division, by any subdivider, of any unit or units of improved or unimproved land, or any portion thereof, shown on the latest equalized county assessment roll as a unit or as contiguous units, for the purpose of sale, lease or financing, whether immediate or future.

See also *Black Hills Invs., Inc. v Albertson's, Inc.* (2007) 146 CA4th 883, 893, 53 CR3d 263 (contracts for sale of two parcels were void; contracts violated Subdivision Map Act because they did not expressly condition sale on approval and filing of parcel map). For discussion of Subdivision Map Act requirements, see California Subdivision Map Act and the Development Process (2d ed Cal CEB 2001).

© The Regents of the University of California

§1.84 (c) Laws on Vested Rights

The lawyers for the parties, especially the purchaser, must be sure to counsel clients on the uncertainty that they will be able to obtain a desired zoning change or even that present zoning will continue. Without specific statutory assurances, a vested right to develop land in a particular way arises only when substantial expenses have been incurred in reliance on a validly issued building permit. See *Avco Community Developers, Inc. v South Coast Regional Comm'n* (1976) 17 C3d 785, 132 CR 386. Statutory assurances are available through development agreements with the local jurisdiction (Govt C §§65864-65869.5), which are enforceable by all parties to the agreement regardless of a change in any applicable general or specific plan, zoning, subdivision, or building regulation adopted by the local jurisdiction. Govt C §65865.4.

Alternatively, developers can obtain a "vesting tentative map" under Govt C §§66498.1-66498.9. An approved vesting tentative map confers a vested right to proceed with development in substantial compliance with the ordinances, policies, and standards in effect at the time the local jurisdiction has found the subdivision application to be complete. Govt C §§66498.1(b), 66474.2. For further discussion of zoning and vested rights, see §§4.85-4.89. On acquiring vested rights, see California Subdivision Map Act and the Development Process, chap 7 (2d ed Cal CEB 2001) and California Land Use Practice, chap 16 (Cal CEB 2006).

© The Regents of the University of California

§1.85 (d) Laws Regulating Foreign Investment and Disposition

With certain exceptions, California requires that 3-1/3 percent of the purchase price be withheld from a seller; however, the seller, on certification, may elect to have a sum withheld equivalent to the amount of actual gain recognized in the transaction. Rev & T C §18662. For discussion of withholding requirements, see §1.89.

© The Regents of the University of California

§1.86 (e) Miscellaneous Applicable Laws

Other state laws and regulatory agencies that may affect a real property sales transaction include the following:

- The Alquist-Priolo Earthquake Fault Zoning Act (Pub Res C §§2621-2630), which requires a special disclosure form for certain properties in earthquake fault areas (see §§4.81, 6.48-6.50).
- The Seismic Hazards Mapping Act (Pub Res C §§2690-2699.6), which requires disclosure for properties located in a seismic hazard zone as designated on maps prepared by the state geologist. See §6.52.
- The California Coastal Act (Pub Res C §§30000-30900), which imposes detailed requirements for approval of any development in the protected coastal zone. Regulations adopted by the Coastal Commission to implement the Coastal Act are set forth in 14 Cal Code Regs §§13001-13666.4. For more detail, see §4.88.
- The Williamson Act (Govt C §§51200-51297.4), which provides property tax incentives for owners of agricultural land who agree with local jurisdictions to maintain agricultural or related uses of land. State reimbursements to counties for these incentives were eliminated by line item veto in the California State budget for fiscal year 2009-2010. For a website on the state budget, see Directory. Existing contracts remain valid, but lawyers and their clients may wish to assess the probability of the renewal of existing contracts and/or new contracts in the current budgetary environment. See §4.93; California Land Use Practice §5.38 (Cal CEB 2006).
- The Cortese-Knox-Hertzberg Local Government Reorganization Act of 2000 (Govt C §§56000-57550), which governs annexation of land through the Local Agency Formation Commission (LAFCO). See §4.91.
- The Metropolitan Transportation Commission Act in the San Francisco Bay Area (Govt C §§66500-66537).
- The San Francisco Bay Conservation and Development Commission (BCDC) (Govt C §§66600-66694).
- The Lake Tahoe Regional Planning Compact (Govt C §§66800-66801).
- · The California Tahoe Regional Planning Agency (Govt C §§67000-67130).
- Any applicable moratorium or similar limitation on development or construction.
- Any applicable historical landmark laws.
- Other laws relating to the condition of the property. See §§1.62-1.64; see also §§4.72-4.82.

© The Regents of the University of California

§1.87 (3) Federal Laws

Federal laws that may affect the purchaser's decisions relating to acquisition of the property include:

- Environmental laws (see §1.88); and
- Laws regulating foreign investment and disposition of real property (see §1.89).

In addition, several other federal laws need to be considered. See §1.90.

© The Regents of the University of California

§1.88 (a) Environmental Laws

The Comprehensive Environmental Response, Compensation, and Liability Act of 1980, widely known by its acronym "CERCLA" (42 USC §§9601-9675), and the Resource Conservation and Recovery Act of 1976 (RCRA) as amended (42 USC §§6901-6992k) are the primary federal statutes dealing with toxic contamination. CERCLA generally addresses releases of hazardous substances and the procedures, costs, and responsibilities for remediating or removing such substances. RCRA regulates the generation, storage, treatment, transportation, and disposal of hazardous wastes. In most real property transactions, CERCLA has the greater impact. See §7.8.

© The Regents of the University of California

§1.89 (b) Laws Regulating Foreign Investment and Disposition

If the client is a non-United States person or entity, review with the client any United States laws (and advise the client to obtain guidance on any laws of the client's home country) that may affect the present purchase or sales transaction. The following are the principal United States laws likely to be pertinent:

- The International Investment and Trade in Service Survey Act of 1976, which requires the periodic filing of reports with the United States Department of Commerce (22 USC §§3101-3108, with implementing regulations at 15 CFR pt 806).
- The Agricultural Foreign Investment Disclosure Act of 1978, which requires the periodic filing of reports on ownership of United States agricultural lands (7 USC §§3501-3508, with implementing regulations at 7 CFR pt 781).
- The Exon-Florio Amendment to the Defense Production Act of 1950, which authorizes the President to investigate and prohibit transactions that "could result in foreign control of any person engaged in interstate commerce" (50 USC App §2170).
- The Foreign Investment in Real Property Tax Act of 1980 (FIRPTA), which applies special federal income tax rules to "foreign persons," as defined in the statute, and also imposes on the purchaser an obligation to withhold 10 percent of the purchase price paid to a seller who is a "foreign person" (IRC §§897, 1445, and regulations promulgated under them). Note that in every transaction in which the seller is not, or claims not to be, a "foreign person," the purchaser should obtain from the seller an affidavit of nonforeign status to assure the purchaser of an exemption under IRC §1445 if the seller's claimed nonforeign status proves to be incorrect.
- Other tax reporting requirements affecting foreign-owned persons, *e.g.,* IRC §§6038A, 6038C; Rev & T C §19135 (information returns on foreign and foreign-owned corporations).

For laws regulating foreign investors in United States real estate, see Smith, Foreign Investment in United States Real Estate (1992).

© The Regents of the University of California

§1.90 (c) Miscellaneous Applicable Laws

Other federal controls include the following:

- The National Environmental Policy Act of 1969 (NEPA) (42 USC §§4321-4370f);
- The Clean Air Act (42 USC §§7401-7671q);
- The Noise Control Act of 1972 (42 USC §§4901-4918);
- The Noise Pollution and Abatement Act of 1970 (42 USC §§7641-7642);
- The Flood Disaster Protection Act (42 USC §§4001-4129);
- The Coastal Zone Management Act of 1972 (16 USC §§1451-1466);
- The Clean Water Act (33 USC §§1251-1387), which prohibits discharging certain materials into "navigable waters"; and
- Title 42 USC §5320, which requires certain historic preservation measures for urban development action grants and may also affect some development projects.

© The Regents of the University of California

§1.91 4. Economic Feasibility of Intended Use

The lawyer should review with the purchaser the various factors that the purchaser will need to consider to assess the economic feasibility of buying the property and putting it to the purchaser's intended use. Items to consider include the following:

- The need for an appraisal of the property (this may be a lender requirement);
- Cost, cash flow, and return-on-investment analyses;
- A tax analysis;
- For currently operating property, a review of the status of current tenancies and historical financial operating results;
- Identification of any additional costs that may be triggered by the change in ownership resulting from the purchase and/or by any postpurchase construction, including property tax reassessment, any required upgrading or renovating for seismic compliance, fire safety, handicapped access, *etc.;*
- Identification of the amounts and terms of any bonds or assessments that are liens on the property;
- If the purchaser's intended use includes leasing the property to others or developing the property and reselling to others, any need for marketing studies;
- Identification of additional costs of purchasing the property and achieving the purchaser's intended use, including design, development, and construction costs; costs of obtaining financing; costs of servicing financing; costs of complying with legal requirements discussed in §§1.72-1.90; and costs of outside experts assisting the purchaser; and
- Identification of any use restrictions applicable to the property. If the property is part of a common interest community, review the governing documents of the community and the governing association, including any covenants, conditions, and restrictions and association articles of incorporation, bylaws, and rules and regulations. On common interest communities, see Advising California Common Interest Communities (Cal CEB 2003) and Forming California Common Interest Developments (Cal CEB 2004).

© The Regents of the University of California

§1.92 5. Consents Needed From Others

The lawyer should review with the purchaser the need for any internal or external consents, as discussed in §§1.66-1.67 with respect to the seller. For a purchaser, the lawyer should be sure to review both the approvals needed to complete the purchase and those needed to accomplish whatever development, construction, or other work that the purchaser will need to perform to put the property to its intended use.

© The Regents of the University of California

§1.93 6. Assist in Engaging Outside Experts

The lawyer should cover the same matters with the purchaser as are discussed in §1.69 with respect to the seller.

© The Regents of the University of California

§1.94 V. STRUCTURING THE TRANSACTION

Early in the process (for a seller, before actively marketing the property; for a purchaser, before making an offer), attention should be paid to the basic structures needed to accomplish the client's needs and objectives.

© The Regents of the University of California

A. Structuring Seller/Purchaser Entities

§1.95 1. Advising the Seller

If all or any part of the property to be sold is owned by a corporation, limited liability company, partnership, or other entity, the lawyer should review the following considerations with the seller:

- If there are multiple entities, will any combinations, split-offs, or other transactions among entities be needed before or as part of the consummation of a sale?
- Are there any adjustments among the interests of the entity owners that must be accomplished before or as part of the consummation of a sale?
- Do the governing documents of the entity contain any special requirements (*e.g.,* approvals by a required percentage of entity owners) or consequences (*e.g.,* required cash distributions or a mandatory termination of the entity on sale) in the event of a sale? Are any amendments to these governing documents prior to a sale necessary or desirable?
- Should the entity (or entities) be dissolved after the sale? Dissolution will involve analyzing both the tax and nontax effects of the sale, both to the entity (or entities) and to its owners.

© The Regents of the University of California

§1.96 2. Advising the Purchaser

The lawyer should review the following considerations with the purchaser:

- If the purchaser is an individual (or group of individuals), the advantages and disadvantages of acquiring the property through an existing or newly formed entity or as cotenants. Tenancy-in-common (TIC) transactions are often used by real estate investors to acquire fractional interests in commercial properties. If structured properly, a TIC investor may defer capital gains using an IRC §1031 exchange. See §1.101. On cotenancies, see §§4.21-4.23; Jacobson, *Tenancy-In-Common*: *An Old Dog Learns New Tricks*, 25 Cal Real Prop J 29 (Winter 2007); Gutierrez, *Drafting and Reviewing Residential Cotenancy Ownership Agreements, Part 1*, 20 CEB Real Prop L Rep 153 (July 1997). For a form tenancy-in-common agreement, see App O.
- The basic choices of entity: subchapter C corporation, subchapter S corporation, general partnership, limited partnership, limited liability company, limited liability partnership. Factors to consider include these:
- Limited liability;
- Tax consequences to the entity owners (with respect to start-up development, loss operations, profitable operations, and later sale or other disposition of the property);
- Management and control; and
- The entity's suitability as a vehicle for allocating a variety of desired economic interests among the various entity owners.
- If the acquisition, ownership, development, operation, and management of the property is to be divided among two or more entities (whether owned by the same group or different groups of investors), the choice of entity in each case and the choice of contractual arrangements between the owner entity and the other entities (*e.g.,* ground lease, operating, or management agreement).
- If the purchaser is an existing entity, whether there is any advantage to acquiring the property through a newly formed entity (either a subsidiary of the existing entity or a new sibling entity, *i.e.,* owned all or mostly by the same persons who own the existing entity).
- If the purchaser will be obtaining debt financing from an institutional or conduit lender, because such lenders generally require the borrowing entity to be a single-purpose entity (SPE), the purchaser and the lawyer should ascertain the lender's entity requirements. For a discussion of SPEs, see California Real Estate Finance Practice: Strategies and Forms, chap 10 (Cal CEB 2000).

Most transfers will result in a reappraisal of the property. Generally, when there is a change in ownership of real property, a new base-year value for the purpose of assessing property taxes is entered on the tax roll. See Rev & T C §50. A "change in ownership," however, does not include a transfer between legal entities "that results solely in a change in the method of holding title to the real property and in which proportional ownership interests of the transferors and transferees, whether represented by stock, partnership interest, or otherwise, in each and every piece of real property transferred, remain the same after the transfer." Rev & T C §62(a)(2). See App A for a discussion of which transfers result in reappraisal. For a discussion of choice of entity issues, see §§4.22-4.28; Organizing Corporations in California §§1.22-1.128 (3d ed Cal CEB 2001); Advising California Partnerships §§1.10-1.23 (3d ed Cal CEB 1999); Forming and Operating California Limited Liability Companies (2d ed Cal CEB 2007).

© The Regents of the University of California

§1.97 B. Structuring the Transaction Itself

The lawyer should review with the client the basic transaction structure that will be most consistent with the client's needs and objectives. This review will enable the client to indicate the desired structure in marketing the property, and it will serve as a reference point in ensuing negotiations. Factors to consider include the matters discussed in §§1.98-1.103.

© The Regents of the University of California

§1.98 1. Choice of Form

The lawyer should review the various forms the transaction might take. The basic choices are:

- An option agreement (see chap 8);
- An agreement of sale with contingencies (see chaps 4, 6); or
- If appropriate in the circumstances,
- a lease with option to purchase; or
- a transaction tailored to a change in the form of the property, as discussed in §1.31.

© The Regents of the University of California

§1.99 2. Liquidated Damages

The lawyer should review the enforceability of liquidated damages clauses and compare it with rules on nonrefundability of option consideration. See §§4.142, 6.10-6.13, 8.75.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/1 Lawyer's Role in Real Property Sales/§1.100 3. Warranties

§1.100 3. Warranties

The lawyer should review strategies for dealing with warranties:

- Title warranties (see §4.111);
- Property condition warranties (see §4.112); and
- "As is" clauses (see §4.120), as limited by law, *e.g.:*
- The laws of fraud and mistake (see California Real Property Remedies and Damages, chaps 3, 11 (2d ed Cal CEB 2002));
- The further limitations under applicable California disclosure statutes (see §§6.9, 6.37); and
- Potential responsibility for contamination cleanup under environmental laws (see §1.64).

The lawyer should consider whether there should be any limit on (1) the number and scope of warranties that survive closing or (2) the aggregate amount of, and the time periods for asserting, postclosing warranty claims.

© The Regents of the University of California

§1.101 4. Tax-Deferred Exchange

The lawyer should always raise with the client the issue of whether a tax-deferred exchange is desirable. Specifically, the Internal Revenue Code provides that neither gain nor loss will be recognized when real property held for productive use in a trade or business or for investment is exchanged solely for like-kind property. IRC §1031(a). Although IRC §1031 generally permits the avoidance of recognition of gain or loss on the exchange of like-kind property, a taxpayer will recognize gain in part when money or other non-like-kind property is also received in the exchange. In other words, a taxpayer who receives money or other non-like-kind property in addition to the like-kind property recognizes gain (but not loss) to the extent of the sum of money or the fair market value of the non-like-kind property received.

The conventional purchase of property with a higher market value generally affords the advantage of greater depreciation. In a tax-deferred exchange, however, that advantage is lost because under IRC §1031(d) the tax basis for the old property determines the basis for the replacement property.

In addition, strict time limits apply with respect to the identification and transfer of exchange property:

- The property to be received in the exchange must be identified within 45 days after the date on which the seller transfers the property to be relinquished in the exchange; or
- The property to be acquired by the taxpayer is received after the earlier of either (1) 180 days after the date on which the seller transfers the property to be relinquished in the exchange; or (2) the due date for the seller's income tax return for the taxable year in which seller's property is sold. IRC §1031(a)(3).

If a seller desires the flexibility to use §1031, a provision should be added to the purchase and sale agreement as discussed in §4.165.

For a comprehensive treatment of the requirements and tax consequences of a tax-deferred exchange, see Real Property Exchanges (3d ed Cal CEB 2002). See also, Kennedy & Baird, *Recent Developments in 1031 Exchanges*, 25 Cal Real Prop J 41 (Summer 2007).

© The Regents of the University of California

§1.102 5. Letter of Intent

The lawyer should consider whether the nature of the transaction is such that a letter of intent should be considered. Some lawyers see no advantage of a letter of intent to a seller, because even when carefully drafted and intended to be a nonbinding outline of the proposed transaction, it may create at least the obligation to negotiate in good faith (a subjective concept whose nuances may be viewed very differently by seller and purchaser). If negotiations break down in disputed circumstances, this obligation can become a cloud on the seller's title. Accordingly, some lawyers believe that a seller should consider a letter of intent only when the purchaser is highly desirable, has a high level of interest, and refuses to negotiate without a letter of intent. Others believe that nonbinding letters of intent are useful tools for both sellers and purchasers. For a detailed discussion of the advantages and risks of using letters of intent, see chap 3.

© The Regents of the University of California

§1.103 6. Client's Ability to be Flexible

The lawyer should review the extent to which (if at all) the client is in a position to depart from the structure most favorable to him or her. For a particular seller, for example, an "as is" transaction in the form of an option may be the only form of transaction the seller is willing to consider. Another seller may prefer one form of transaction but may be in a position (or forced by circumstances) to consider other forms as well. It is important for both the lawyer and the client to have a clear sense at the outset of where the client's individual situation lies on this spectrum of possibilities.

© The Regents of the University of California

VI. STRUCTURING AND COORDINATING THE MARKETING PROCESS

§1.104 A. Marketing Considerations to Review With Seller

Occasionally, a seller will have little choice in how the property is to be marketed. If the seller is an estate or is a bankrupt with a trustee appointed, for example, it may be necessary to conduct a probate sale or a trustee's sale according to the applicable rules governing such sales. Even in cases of estates and bankruptcies, however, a choice may be available; in most other situations there clearly will be a choice. The essential choices are discussed in §§1.105-1.108.

© The Regents of the University of California

§1.105 1. Brokered or Nonbrokered Sale

The issue of whether to have a brokered or a nonbrokered sale turns on the extent to which a broker's involvement will (1) provide more market exposure than the seller could otherwise achieve and (2) relieve a seller desiring relief from the logistical chore of marketing the property. See §§2.23-2.24.

© The Regents of the University of California

2. Negotiated Sale or Sale Involving Bidding

§1.106 a. Estate

For an estate, the issue in choosing the type of sale is whether it appears necessary (*e.g.,* because of disputes among beneficiaries) or desirable (because of the potential for overbidding for this particular property) to conduct the sale as a probate sale in which an accepted offer would be subject to bidding in open court.

NOTE: If a probate sale is contemplated and a broker will be engaged, be aware that (1) the broker's commissions will be subject to the court's approval (including possible adjustment) and (2) complex rules govern the payment of brokerage commissions if there is a broker-assisted successful overbidder (see Prob C §§10161-10168). Make sure the broker agreement is subject to those approvals and rules.

© The Regents of the University of California

§1.107 b. Nonestate

Even when no estate is involved, there may nevertheless be circumstances in which it is desirable to consider structuring the sale as one involving bidding. It especially makes sense to consider such a structure during times of rising prices and high purchaser demand. During "buyers' markets," bidding structures are rarely seen as they require multiple parties to be interested simultaneously in purchasing a property and allow less flexibility in contract structure.

NOTE: The secrets to a successful private bidding sale are to (1) spell out in detail, in advance and in writing, the rules for each step of the process, and (2) adhere faithfully to those rules. Moreover, if a bidding sale is contemplated and a broker will be engaged, be sure that such a sale is provided for in the brokerage agreement. Some brokers do not want to be involved in bidding sales, and it is only fair to bring that issue to the table at the outset.

© The Regents of the University of California

§1.108 3. Anticipating Multiple Offers

It is important for the seller to decide, first, what rules to follow if multiple offers are made, and then to make sure to clearly communicate those rules to any broker involved and to each prospective purchaser. Most important is to establish the rule that the seller reserves the right to consider (or not consider) any offer submitted at all times before the time an offer is ultimately accepted. If the seller decides to make a counterproposal to a particular offer, the seller should also decide whether the counterproposal is to be subject to a continuing right by the seller to consider other offers (*i.e.,* the seller can continue to negotiate with others, and there is to be no deal with this offeror unless and until the final terms are accepted by the seller). If such a condition is to apply, it should be clearly stated in the counterproposal. This condition is extremely important in maintaining control of the marketing process and avoiding the nightmare of being bound by contract to more than one purchaser.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/1 Lawyer's Role in Real Property Sales/§1.109 B. Marketing Considerations to Review With Purchaser

§1.109 B. Marketing Considerations to Review With Purchaser

Although the seller's decisions, discussed in §§1.105-1.108, may limit the available choices, the purchaser may still have some options. See discussion in §§1.110-1.113.

© The Regents of the University of California

§1.110 1. Separate Broker

The issue for the purchaser turns on the extent to which the purchaser needs to engage a broker to help in locating a suitable property.

NOTE: If the purchaser decides to engage a broker, make sure the broker agreement is clear about the circumstances in which a commission is earned and about who will pay it. Remember, too, that the seller is not a party to the agreement between the purchaser and the purchaser's broker. If the understanding is that the compensation of the purchaser's broker is to be paid by the seller, an agreement by the seller to pay that compensation must be included in the purchase contract. See chap 2.

© The Regents of the University of California

2. Negotiated Sale Versus Bidding Sale

§1.111 a. Estate

The purchaser's objective will usually be to avoid open-court bidding. If the seller is determined to have a bidding sale, then the purchaser has no choice. To test the seller's intent, however, the purchaser should explore alternatives with the seller (*e.g.,* a private sale under the independent administration rules, or distribution of the property to, and then sale by, the estate beneficiaries).

© The Regents of the University of California

§1.112 b. Nonestate

The purchaser's position in a nonestate context is purely a matter of bargaining power. If the purchaser has bargaining leverage, the seller may be dissuaded from having a private auction. If the seller is determined to have an auction, the purchaser's essential choices are to play (perhaps with some say in what the rules are to be) or to move on to another property.

© The Regents of the University of California

§1.113 3. Anticipating Multiple Offers

The purchaser's objective is essentially the reverse of the seller's: A purchaser who submits an offer wants to have the seller negotiate exclusively with the purchaser until a sale is either made or abandoned. As with bidding, the purchaser's position essentially depends on the purchaser's bargaining power. A purchaser who feels in a strong bargaining position should look at two alternative approaches:

- In a major transaction, the lawyer should consider proposing a letter of intent that includes an exclusive negotiation provision. See chap 3 on letters of intent.
- In a transaction in which a letter of intent is inappropriate, the lawyer should consider including a provision in the offer that the offer is subject to the requirement of exclusive negotiation. This approach does not bind the seller (who can reject the offer or reply with a counterproposal that rejects the exclusive negotiation condition), but it makes the purchaser's position clear and, if the seller is sufficiently motivated to deal with the purchaser, may produce the intended result (*i.e.,* a period during which negotiations with the purchaser are exclusive).

© The Regents of the University of California

§1.114 VII. STRUCTURING AND COORDINATING THE NEGOTIATION AND DOCUMENTATION PROCESS

Depending on the client's needs and objectives, the lawyer can play a variety of roles in the planning, organization, and management of the marketing and negotiation process. These roles include the following:

- Organizing the negotiating team (see §1.115);
- Conducting negotiations (see §§1.116-1.118);
- Generating the transactional documents (see §§1.119-1.120);
- Rendering legal opinions (see §§1.121-1.130); and
- Structuring and coordinating the closing process (see §§1.131-1.139).

© The Regents of the University of California

§1.115 A. Organizing the Negotiating Team

Depending on the circumstances, the "team" may consist of just the lawyer and the client, or it may consist of any number of additional people, including employees of the client and various outside experts retained to assist the client in the transaction. The key requirements are:

- The team should include all persons needed to achieve the result desired by the client;
- There should be clear lines of communication and job definitions among the members of the team;
- One member (or as few members as possible) should be designated to handle communications relating to negotiations with any prospective other party to the transaction; and
- A team leader should be designated to be responsible for coordinating the work of the team.

© The Regents of the University of California

§1.116 B. Conducting Negotiations

The appropriate role for the lawyer will depend on the circumstances and can range from advising the client from the background to playing the lead role in the negotiation process.

On negotiating title insurance with the title company, see California Title Insurance Practice §§2.22-2.27 (2d ed Cal CEB 1997).

© The Regents of the University of California

§1.117 1. Other Counsel

When one or more other parties to the transaction are represented by counsel, the Rules of Professional Conduct require that the lawyer communicate with that counsel unless that counsel consents to direct communications with the client. Cal Rules of Prof Cond 2-100. If a material party to the transaction is not represented by counsel, consider the advisability of requesting that that party obtain counsel. The enforceability of the agreements reached in negotiations may be affected by whether that party needs counsel's assistance to fully understand the provisions of the agreements.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/1 Lawyer's Role in Real Property Sales/§1.118 2. Attorney's Role in Negotiation Process

§1.118 2. Attorney's Role in Negotiation Process

Regardless of the nature and scope of the lawyer's role, it should encompass the same essential contributions to the process. The lawyer should

- keep testing the progress of negotiations against the client's needs and objectives;
- assist the client in recognizing issues that affect those needs and objectives;
- assist the client in finding workable solutions to disputed issues; and
- regardless of how emotional the other parties to the process may become, maintain a composed manner and a firm and objective grasp on where the negotiations stand in order to guide the client to a resolution of issues (or an informed and well-reasoned conclusion that certain issues cannot be resolved).

© The Regents of the University of California

C. Generating Transactional Documents

§1.119 1. Drafting and Adapting Forms

In drafting or revising the transactional documents, the lawyer bears a heavy responsibility for producing documents that achieve the parties' wishes. The various forms available can be valuable drafting tools, but caution must be exercised when using them. Forms that lawyers frequently use include the following:

- Printed forms with blanks to be filled in, such as the California Association of Realtors® (CAR) exclusive authorization and right-to-sell form (see §2.57) and residential purchase agreement and receipt for deposit (see chap 6);
- Forms in form books (and books such as this one), which can be adapted for a particular transaction; and
- Form documents retained in the lawyer's files or computer files from previous transactions.

The hazard in using ready-made forms instead of tailoring instruments to each situation is that they may be used uncritically and with insufficient attention to the comments that accompany them or to the reasons for using particular language. No ready-made form is a substitute for a document designed for the particular client's situation. Nor can any form, however perfect it may have been when originally designed, remain equally dependable in the face of changing times and laws. When computer-generated or electronically generated forms are used, the hazard is magnified by the ease with which lengthy documents can be stored and then retrieved and modified for use in subsequent transactions. The lawyer must remember to recheck the *entire* form to make sure that a provision that does not fit the present transaction is deleted or changed as appropriate.

Nevertheless, there are sound legal and economic reasons for using forms in drafting instruments. Even if it is substantially supplemented and revised, a good form can provide a basis for the drafting process, especially when a new problem arises. Each of the basic types of form is a kind of checklist, protecting against inadvertent omission of necessary or desirable clauses. Moreover, a well-worded form offers protection against ambiguities that may result from drafting under a deadline. On the economic side, struggling anew with legal problems, organization, and special phrasing is a waste of productive time when these issues have already been carefully worked out.

Forms should be used with respect for their constructive uses but with awareness of their dangers. The forms should be chosen carefully and reviewed critically; annotations should be filed with office forms; drafting should be done only after reading the comments and annotations that accompany the forms; and the forms should be adapted to precisely meet the needs of the new situation.

© The Regents of the University of California

§1.120 2. Standard Forms; Boilerplate

The lawyer should keep in mind (and make sure the client understands) that there are no such things as "standard forms" and "boilerplate." All provisions of a real property contract, whether typed or preprinted, are appropriate subjects for negotiation, and changes to forms should be made whenever needed to tailor the form to the terms of an acceptable deal.

PRACTICE TIP: Because changes in laws may alter the effect of form provisions, and because publishers have their own biases and may revise their forms over time, the lawyer should not assume that a form's provisions are "reasonable" or represent a compromise of the buyer's and seller's perspectives. Indeed, given the increasing ease with which documents may be manipulated electronically, the lawyer should not assume that a form that seems familiar in fact contains the language that he or she expects.

© The Regents of the University of California

D. Rendering Legal Opinions

§1.121 1. Contexts in Which Legal Opinions Arise

The lawyer handling a real property sales or purchase transaction may encounter legal opinions in a variety of contexts. For example:

- The client may request a written opinion on one or more aspects of the transaction.
- If a government agency is in some way involved in the transaction (or in the development or other use of the property after the transaction closes), the agency may request a written opinion on one or more issues relating to its involvement.
- If the purchaser is borrowing or raising equity money to fund the purchase, the lender or investors may request a written opinion on a variety of issues bearing on the validity and enforceability of the funding documents (and sometimes certain aspects of the underlying transaction).
- If the purchaser is obtaining debt financing, the lender will typically require the lawyer for the purchaser-borrower to provide a legal opinion as to the borrowing entity and the enforceability of the loan documents.
- Opinions on title matters may be requested by the purchaser, but it is customary for the purchaser to rely on title insurance for assurances as to title matters.

NOTE: The lawyer may be on either end of the request (*i.e.,* the one who is asked for an opinion or the one asking the other party's lawyer for an opinion) or may be involved in both activities.

© The Regents of the University of California

§1.122 2. How to Know an Opinion When You See One

Lawyers should be aware that their written response to a request for their views or state of knowledge on a particular point might well be treated as a legal opinion. Although it will usually be clear that an opinion is intended, the nature of the request or the context in which it is made may make it difficult to know what is intended and how the matter should be handled.

For a compilation of reports on opinion letters (some superseded by the 2005 Report cited at the end of this section), see Executive Committees of the Business Law and the Real Property Law Sections of the California State Bar, The 2002 California Opinion Reports, State Bar of California (2002) (cited as California Opinion Reports (2002)); the publication is available to State Bar members on the State Bar website, which is listed in the Directory. The California Opinion Reports (2002) contains reports and addendums for and from 1989-2002. Also, some useful rules of thumb are suggested by the discussion in the Legal Opinions in Business Transactions (2005 Report), The Corporations Committee of the Business Law Section of the State Bar of California, superseding the 1989 Report.

© The Regents of the University of California

§1.123 a. Watch for Writings in Legal Opinion Contexts

The term "opinion" is variously defined, depending on the context in which it is used. See the 2002 California Opinion Reports, State Bar of California (2002), and the Legal Opinions in Business Transactions (2005 Report), The Corporations Committee of the Business Law Section of the State Bar of California; the publication is available to State Bar members on the State Bar website, which is listed in the Directory. See also §1.122.

In a general context, the 2005 Report cites two dictionary definitions of "opinion" at Part II, n25:

- A Webster's definition: "a formal expression by an expert (as a professional authority) of his thought upon or judgment or advice concerning a matter."
- A Black's Law Dictionary definition: "[a] written document in which an attorney provides his or her understanding of the law as applied to assumed facts."

In the context of a business transaction, the 2005 Report defines a legal opinion as a formal writing prepared by an opinion giver, expressing an informed understanding of the legal principles generally applicable to a specific transaction or to a particular aspect of such a transaction.

As a rule of thumb, these definitions suggest that if a lawyer is asked to prepare any writing in any of the circumstances addressed in these definitions, the lawyer should assume that the writing will be construed as a legal opinion and that the degree of care required for such an opinion applies to that writing.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/1 Lawyer's Role in Real Property Sales/§1.124 b. Watch for 'Factual,' 'Reasoned,' and 'Comfort' Opinions

§1.124 b. Watch for "Factual," "Reasoned," and "Comfort" Opinions

The Legal Opinions in Business Transactions (2005 Report), The Corporations Committee of the Business Law Section of the State Bar of California, Part IV(B)(1) (available to State Bar members on the State Bar website, which is listed in the Directory) contains excellent discussions of the difficulties arising in three common gray areas:

- When the requested writing covers matters that are essentially factual in nature (sometimes referred to as "factual opinions");
- When the request is for legal conclusions on matters in which there is some recognized legal uncertainty (so-called reasoned opinions); and
- When the request is for written confirmation that the lawyer knows of no misstatements or omissions in the client's representations (so-called comfort opinions).

Because of the difficulties these opinions present, the lawyer should generally avoid them whenever possible and, when they cannot be avoided, take particular care to qualify them in the manner discussed in the 2005 Report. See also §1.123.

© The Regents of the University of California

§1.125 c. Avoid Unnecessary Opinions

Legal opinions are laborious to produce. Although much of the factual due diligence and legal research required to prepare a proper legal opinion will have already been performed in order to handle the transaction properly, an opinion may involve extra due diligence or research, especially on any matters that—without the need to render an opinion on them—would not have been within the scope of the lawyer's engagement. Additional time will also be involved in crafting the opinion and, no doubt, in negotiating the scope and precise wording of the opinion with counsel on the other side. All this extra activity will add to the client's transaction cost, and yet the technical nature of the matters covered in the opinion will often make it difficult for the client to understand how the opinion (and the process of preparing it) add any value to the transaction. It is therefore a useful (and obvious) rule of thumb to avoid giving or requesting unnecessary legal opinions. In many contexts, it may be appropriate to have no legal opinions at all. In other situations, legal opinions on certain matters may be necessary, but the scope of the matters covered (and thus the amount of effort involved in preparing the opinion) can be narrowed to only those matters that are clearly necessary.

© The Regents of the University of California

§1.126 3. Legal Standards Applicable to Opinions

Although there is currently no developed law or Bar canon specifically setting standards for the preparation of legal opinions, the lawyer should expect that the professional responsibilities discussed in §§1.3-1.12 apply to the preparation and issuance of legal opinions with the same force as to the lawyer's other legal services. See Legal Opinions in Business Transactions (2005 Report), The Corporations Committee of the Business Law Section of the State Bar of California; the publication is available to State Bar members on the State Bar website, which is listed in the Directory (see also §1.123).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/1 Lawyer's Role in Real Property Sales/§1.127 4. Essential Resources Available to the Attorney

§1.127 4. Essential Resources Available to the Attorney

A substantial body of helpful literature exists to assist lawyers in understanding

- the function of legal opinions;
- how to word them; and
- how to structure the research and factual due diligence required to render such opinions properly.

Some of the best resources on legal opinions are listed in the selected bibliography in Appendix C to the Legal Opinions in Business Transactions (2005 Report), The Corporations Committee of the Business Law Section of the State Bar of California; the publication is available to State Bar members on the State Bar website, which is listed in the Directory (see also §1.123). A useful addition to this literature is Glazer & FitzGibbon on Legal Opinions (2d ed 2001), which includes substantial discussion of third party legal opinions, copies of the Bar reports discussed in §1.129, several other non-California Bar reports, and an exhaustive annotated bibliography. See also Preble, *The Remedies Opinion Revisited*: *A Primer for Real Estate Lawyers*, 33 ABA Real Prop, Prob & Trust J 63 (Spring 1998).

© The Regents of the University of California

§1.128 a. State Bar Reports

The presently available literature includes several State Bar reports (and an addendum to one of them) that are indispensable resources. Although they overlap somewhat in their discussions, overall they complement each other and all of the reports should be on every lawyer's bookshelf. Collectively, they deal extensively with the nature and purpose of legal opinions, the elements to be included in legal opinions (in many cases with examples of specific language used by various practitioners), and discussions of many of the more difficult opinion areas. They also include references to virtually all relevant case law and literature available on the subject of legal opinions at the time the reports were written. The reports, which are collected in a volume titled 2002 California Opinion Reports (2002) that is available for purchase from the State Bar (see Directory), include (see also §1.123):

- *1995 California Real Property Opinion Report*, 13 Cal Real Prop J 1 (Fall 1995) and *First Supplement to 1995 California Real Property Opinion Report*, 16 Cal Real Prop J 15 (1998).
- *Report on the Adaptation of the Legal Opinion Accord of the Section of Business Law of the American Bar Association for Real Estate Secured Transactions, Section of Business Law of the American Bar Association and the American College of Real Estate Lawyers* (1993), 29 ABA Real Prop, Prob & Tr J 569 (Fall 1994). This report was revised and republished as A Report of the Joint ABA/ACREL Committee Comprising: The American Bar Association, Section of Real Property, Probate and Trust Law, Committee on Legal Opinions in Real Estate Transactions, Subcommittee on Creation of an Inclusive Opinion, and the American College of Real Estate Lawyers Attorneys' Opinion Committee.
- Former 1989 Report of the Committee on Corporations of the Business Law Section of the State Bar of California Regarding Legal Opinions in Business Transactions (Aug. 31, 1989), revising and updating the earlier report published by the committee in 1982.
- *Legal Opinions in California Real Estate Transactions, A Joint Committee Report by the Real Property Law Section of the State Bar of California and the Real Property Section of the Los Angeles County Bar Association*, 42 Bus L 1139 (1987), plus Legal Opinions in California Real Estate Transactions: An Addendum (Mar. 14, 1990).
- *Report of the Uniform Commercial Code Committee Regarding Legal Opinions in Personal Property Secured Transactions, Business Law Section of the State Bar of California* (Dec. 1988), revising and updating an earlier report published on December 31, 1986.

The 1995 report, published in the California Real Property Journal (see first bullet above), comments on the ABA Report and the ABA ACREL Report referred to in §1.130:

- *Report of a Joint Committee of the Real Property Section of the State Bar of California and The Real Property Section of the Los Angeles County Bar Association on the Legal Opinion Reports of (I) The ABA Section of Business Law, and (II) The ABA Section of Real Property, Probate and Trust Law and The American College of Real Estate Lawyers* (Fall 1995) (referred to in this book for brevity as the 1995 California Report).

NOTE: The Business Law Section has also published the Report on Third-Party Remedies Opinions (Sept. 2004). This Report updates portions of the Business Law Section's 1989 Report as well as the Section's 1992 Report on the Third-Party Legal Opinion Report of the ABA Section of Business Law. This 2004 Report, in conjunction with Legal Opinions in Business Transactions (2005 Report), The Corporations Committee of the Business Law Section of the State Bar of California, superseding the 1989 Report, provides further guidance to California lawyers about practices regarding remedies opinions. A 2007 update on the Report on Third-Party Remedies Opinions currently is available only online at the State Bar website (see Directory for address).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/1 Lawyer's Role in Real Property Sales/§1.129 b. ABA Reports

§1.129 b. ABA Reports

Three important additions to the available literature are the following:

- The *Third-Party Legal Opinion Report, Including the Legal Opinion Accord, of the Section of Business Law, American Bar Association*, 47 Bus Law 167 (Nov. 1991) (formally cited as the ABA Legal Opinion Report, but for brevity referred to in this book as the ABA Report). This report is available for purchase from the American Bar Association at the address provided in the Directory.
- The Business Law Section of the State Bar of California Report on the Third-Party Legal Opinion Report of the ABA Section of Business Law (May 1992) (formally cited as the California Report on the ABA Report, but for brevity referred to in this book as the California Response). This report is available for purchase from the Business Law Section of the State Bar of California at the address provided in the Directory.

NOTE: Report on Third-Party Remedies Opinions, published by the Business Law Section of the State Bar (Sept. 2004), updates portions of the California Response. A 2007 update on the Report on Third-Party Remedies Opinions currently is available only online at the State Bar website. (For information on ordering this report and accessing the update for free, see Directory.)

- *Report on Adaptation of the Legal Opinion Accord of the Section of Business Law of the American Bar Association for Real Estate Secured Transactions*, published in 29 ABA Real Prop, Prob & Trust J at 569 (Fall 1994) (referred to in this book for brevity as the ABA ACREL Report).

© The Regents of the University of California

§1.130 c. Accord

The ABA Report (see §1.129) contains an accord (in the ABA Report this is called the "Accord"; among practitioners, it is often referred to as the "Silverado Accord," after an ABA Business Law Section conference held early in the deliberation process in Silverado, California). The Accord sets forth specific position statements on a number of definitions, procedures, and limitations. If the Accord is adopted in an opinion, then these definitions, procedures, and limitations govern the opinion and need not be separately stated. The California Response (see §1.129) contains a helpful discussion of the background of the ABA Report and discusses several respects in which the positions stated in the Accord are at odds with the approaches taken in the California Bar's former 1989 Report (see §1.128).

The ABA ACREL Report (see §1.129) adapts the ABA Report for use in real estate secured financing transactions, and the 1995 California Report provides a California response and commentary to the ABA Report and the ABA ACREL Report. (see §1.128).

Both the ABA Report and the California Response emphasize that use of the Accord is consensual (*i.e.,* a matter of agreement between the parties to a particular transaction) and that neither the ABA Report nor the Accord itself is to be used as a frame of reference for evaluating or interpreting opinions delivered in the past or those delivered in the future that do not adopt the Accord.

The Accord generally has not been fully embraced in California legal opinions given in real estate secured transactions. To take advantage of the refinements in the California Report, the ABA ACREL Report, and the 1995 California Report, it is necessary to incorporate all or portions of those reports in an opinion that adopts the Accord. The nature and structure of the reports and the Accord make such incorporation a rather unwieldy process, and most opinions rendered today still set forth the relevant definitions and qualifications in full in the body of the opinion letter. Nevertheless, the reports are a valuable and necessary resource for California attorneys who render legal opinions, and they are an important component of the available body of literature on legal opinions.

For an in-depth discussion of the ABA-ACREL opinion used in secured loan transactions, see California Real Estate Finance Practice: Strategies and Forms, chap 8 (Cal CEB 2000). For a more up-to-date report, see Report on Third-Party Remedies Opinions, State Bar of California Business Law Section (Sept. 2004) and the 2005 Report (see §§1.123, 1.129).

© The Regents of the University of California

VIII. STRUCTURING AND COORDINATING THE CLOSING PROCESS

A. Organizing and Coordinating Escrow

§1.131 1. Understanding the Process

The lawyer should make sure that the client understands how the escrow process works (experienced real property sellers or purchasers generally do understand, but occasional sellers or purchasers often do not). In discussing the escrow process with the client, the lawyer should

- review the differences between escrow functions and title insurance functions;
- make sure the client understands that once money (and/or documents) have been deposited in escrow, even if under clear instructions entitling the client to have these items returned on demand, an escrow holder concerned about its position if a dispute arises may refuse to return them unless all parties to the escrow consent, and will usually file an interpleader action so that a court resolves the dispute (CCP §§386-386.6).

On escrows generally, see chap 15.

© The Regents of the University of California

§1.132 2. Written Escrow Instructions; Follow-Up

The lawyer should make sure that all facets of the escrow holder's activities are covered by clear and complete written escrow instructions and then follow up the instructions with whatever further communications—written and verbal—are needed to ensure that the instructions were correctly understood and are being correctly carried out. The lawyer should not assume that the escrow instructions, as clear as they may be, will be strictly followed. Escrow offices are busy places, and misunderstandings and errors do occur. Escrow should be organized so that either the lawyer or another responsible member of the "team" will review all steps of the closing process with the escrow holder, check all closing documents deposited in escrow, and actively monitor the closing to ensure that the instructions are, in fact, implemented as written. See chap 15.

On written title instructions and for form title instructions, see California Title Insurance Practice §§10.13-10.18 (2d ed Cal CEB 1997).

© The Regents of the University of California

§1.133 B. Advising Client on Title Insurance

Title insurance is a normal part of most real property purchase transactions (and in the author's view, should be regarded by both purchaser and seller as a necessary element of any such transaction). Yet it is amazing how many clients (and often their expert advisers) do not fully understand how title insurance works and the choices that are available among title insurance products. The points the lawyer should review with the client include the matters discussed in §§1.134-1.139. See also California Title Insurance Practice §§2.1-2.39 (2d ed Cal CEB 1997).

© The Regents of the University of California

§1.134 1. Choice of Basic Policy Forms

The lawyer should review the basic coverages and exclusions from coverage provided by the standard California Land Title Association (CLTA) owner's policy form, the CLTA/ALTA Homeowner's Policy, and the extended coverage American Land Title Association (ALTA) owner's policy form. As part of this review, note the key coverage differences between the two forms.

In 2006, ALTA adopted new and updated versions of the owners and loan title insurance policies. For a summary of the changes, see Cruz, Hammann & Rogers, *The New 2006 ALTA Policies*: *The Industry Listens!*, 24 Cal Real Prop J 3 (Fall 2006). For in-depth discussion and comparison of ALTA and CLTA policies, including the 2006 policies, see California Title Insurance Practice, chap 6 (2d ed Cal CEB 1997). On owner's policies, see Title Ins, chap 7.

© The Regents of the University of California

§1.135 2. Addressing Particular Problems

The lawyer should review any particular problems areas that may be involved in the transaction, including, *e.g.,* the following:

- Matters not covered by the type of policy (whether CLTA or ALTA) that the client proposes to obtain (see California Title Insurance Practice, chaps 6-7 (2d ed Cal CEB 1997).
- Techniques for dealing with problems that cannot easily be removed before closing (*e.g.,* disputed mechanics' liens).
- If applicable, confirmation of coverage against the special (and unrecorded) state and federal estate tax liens.
- Review of what it means to "insure around" an exception (*i.e.,* the policy insures against loss arising from the exception, but the exception itself remains a burden on the title to the property). This arrangement may be acceptable in some cases but not in others. For further discussion of insuring around particular problems, see Title Ins §§4.28, 7.84-7.85.

© The Regents of the University of California

§1.136 3. Policy Endorsements

If applicable, the lawyer should review the function and availability of policy endorsements and consider whether any particular problems can be met by appropriate endorsements. On owner's endorsements, see California Title Insurance Practice §§7.64-7.103 (2d ed Cal CEB 1997). On lender's endorsements, see Title Ins §§8.50-8.118.

For a chart of available CLTA endorsements, see Title Ins, App I.

© The Regents of the University of California

§1.137 4. Wording of Policy Provisions

The lawyer should recognize that the particular wording of policy exceptions and additional title endorsements can be negotiated with the title company. Refinements in wording can be important in making sure that the exception clearly and correctly identifies only the particular title condition and does not imply other problems or conditions. Changes in wording may also be appropriate if the title insurer is willing to enlarge the coverage of the policy by narrowing the scope of the exception. An example of the latter situation is a modification of the usual exception for supplemental tax liens to have the exception apply only to supplemental taxes arising after closing (thereby extending the coverage of the policy to any liens arising from changes of ownership or construction occurring prior to closing). Wording changes to correct or clarify the policy are also appropriate in the other nonprinted parts of the policy, including legal descriptions, characterization of the vested estate, and the contents of policy endorsements.

On negotiating coverage, see California Title Insurance Practice §§2.22-2.27, 5.21-5.24 (2d ed Cal CEB 1997).

© The Regents of the University of California

§1.138 5. Insurer's Financial Ability

Title insurance is like other insurance—an indemnification by the title insurer against losses covered in the insurance contract. As with any insurance policy, the lawyer must consider the financial resources of the underwriting title insurer in relation to the amount of risk covered. If the insuring company's financial resources are of concern, consider spreading the risk by requiring the principal underwriting company to reinsure specified amounts of the total policy liability with other acceptable title insurers.

On evaluating the financial stability of the title insurer, see California Title Insurance Practice §§3.6-3.10 (2d ed Cal CEB 1997).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/1 Lawyer's Role in Real Property Sales/§1.139 6. Policy Costs and Required Lead Times

§1.139 6. Policy Costs and Required Lead Times

The lawyer should be aware of the requirements for the policy to be obtained, including any additional costs or lead times involved. The lawyer should consider, *e.g.,* the following:

- The extra cost and time required to obtain the ALTA survey required for an extended-coverage ALTA owner's policy (on ALTA surveys, see California Title Insurance Practice §4.32 (2d ed Cal CEB 1997);
- Any documentation required by the title company to verify the authority of persons acting for a trust, corporation, partnership, or other entity (on establishing authority to act, see Title Ins §§2.29-2.35); and
- Any documentation required by the title company to remove an unwanted exception (on negotiating exceptions and handling title defects, see Title Ins §§5.21-5.24, 5.39-5.44).

On title insurance premiums and methods of reducing premiums, see Title Ins §§3.15-3.27.

© The Regents of the University of California

IX. POSTCLOSING FOLLOW-UP

§1.140 A. Making Sure All Closing Details Are Complete and Correct

After close of escrow, the lawyer's involvement in other matters related to the transaction or the property varies according to the scope of the lawyer's engagement. See §§1.17-1.18. Such matters are generally beyond the scope of this chapter, but the client usually contemplates at least some follow-up on matters that may reasonably be considered an integral part of the transaction. If the lawyer believes that such follow-up activities are not part of the engagement (and this limitation is not already clear in the lawyer's engagement letter with the client), the lawyer should make sure that the client knows (preferably through a written communication) that the lawyer will not be attending to those matters.

© The Regents of the University of California

§1.141 B. Examples of Follow-Up Matters

The number and kind of postclosing follow-up matters vary from transaction to transaction. Examples of frequently encountered matters include the following:

- Receipt and review of title policy (see §1.142);
- Receipt and review of other closing documents (see §1.143); and
- Monitoring certain postclosing notices and actions (see §1.144).

© The Regents of the University of California

§1.142 1. Receipt and Review of Title Policy

Although the title policy will be issued as of the closing date, title companies rarely have the policy form physically completed and ready for delivery at the closing. Follow-up is needed to ensure that the policy is issued as soon as practicable after the closing and that the policy, as issued, is correct. The latter point is extremely important. Mistakes do happen, and the process of correcting a mistake in the policy will be easier (and more likely to be successful) if the mistake is brought to the insurer's attention soon after the closing rather than months (or years) later. On reviewing the title policy, see California Title Insurance Practice §§10.20-10.21 (2d ed Cal CEB 1997).

© The Regents of the University of California

§1.143 2. Receipt and Review of Other Closing Documents

Although most closing documents will have been delivered to the parties at the closing, there may be some documents not physically delivered to the parties at that time. It may have been convenient to ask the escrow holder to mail (or deliver by other means) some or all of the closing documents after closing. Also, any recorded documents remain at the recorder's office until processed and are then mailed to the addressee shown on the face of the document. Follow-up is needed to ensure that all documents are in due course received and, when received, are still in the proper condition.

© The Regents of the University of California

§1.144 3. Monitoring Certain Postclosing Notices and Actions

Certain notices may need to be given or other actions may need to be taken after closing that are time sensitive and closely connected to the transaction itself. Examples include:

- Following up the postclosing disposition of an escrow holdback for, *e.g.,* discharge of a disputed mechanics' lien claim or payment for repair work;
- Obtaining refund from the escrow holder of any unused balance of the funds deposited by the purchaser in escrow;
- If the seller has remained on the property under a short lease or a rental arrangement, monitoring the termination or expiration of that lease or arrangement; and
- If the purchase and sale agreement contains indemnification provisions requiring the purchaser to assert claims within a short specified period after closing, making sure that the purchaser anticipates the specified deadline and, if the purchaser does have claims, that they are filed within the time and in the manner specified in the agreement.

© The Regents of the University of California

2

Brokers

Randall I. Barkan
Jeffrey H. Belote

I. REGULATION OF BROKERS §2.1
- A. Licensing §2.2
  - 1. Licensing Qualifications §2.3
  - 2. Corporations and Partners as Licensees §2.4
  - 3. Brokers Distinguished From Finders §2.5
  - 4. Exemptions From Licensing Requirements §2.6
- B. Specialized Licensees
  - 1. Mortgage Loan Brokers §2.7
    - a. Disclosure Requirements and Limits on Charges §2.8
    - b. Disclosure and Compliance Requirements for Nontraditional and Subprime Mortgage Products §2.8A
    - c. SB 94 and AB 260 §2.8B
    - d. Exemption From Usury for Loans Made or Arranged by Broker §2.9
  - 2. Business Opportunity Brokers §2.10
  - 3. Real Estate Syndicate Securities Dealers §2.11
- C. Real Estate Advertising §2.12
- D. Interpretive Opinions §2.12A
- E. Broker's Relationship With Salespersons
  - 1. Salesperson Licensing and Employment Requirements §2.13
  - 2. Supervision of Salespersons §2.14
    - a. Relationship Between Broker and Salesperson Under Bus & P C §10032 §2.15
    - b. Relationship Between Broker and Salesperson Under Common Law and Other Statutory Schemes §2.16
    - c. Unemployment Insurance §2.17
    - d. Worker's Compensation §2.18
    - e. Withholding Income and Social Security Taxes §2.19
    - f. Tort Liability §2.20
  - 3. Documenting Relationship Between Broker and Salesperson §2.21
- F. Broker as Escrow Agent
  - 1. License Requirements §2.22
  - 2. Decision to Use Broker-Escrow Agent §2.23

II. BROKERS' SERVICES; SELECTING A BROKER
- A. Type of Services §2.24
- B. Factors to Consider in Selecting a Broker §2.25

III. BROKER AS AGENT
- A. Agency Versus Contract Law §2.26
- B. Creation of Agency Without Written Contract §2.27
  - 1. Agency by Express or Implied Agreement §2.28
  - 2. Agency by Ratification §2.29
  - 3. Ostensible Agency §2.30
- C. Residential Disclosure Requirements on Agency Relationship
  - 1. Disclosure of Agency and Confirmation Forms §2.31
  - 2. Failure to Comply With Agency Disclosure Requirements §2.32
  - 3. Agency Elections §2.33
  - 4. Change in Agency Election §2.34
  - 5. Dual Agency of Listing Agents §2.35
  - 6. Form: Disclosure of Agency Relationship (CC §2079.16) §2.36
  - 7. Form: Confirmation of Agency Relationship (CC §2079.17) §2.37
- D. Unintended Dual Agency §2.38
- E. Broker Acting in Non-Agency Capacity §2.38A

F. Multiple Listing Service §2.39
1. Subagency §2.40
2. Nonmember Access to Multiple Listing Services §2.41
G. Extent of Broker's Authority to Bind Principal §2.42

IV. CONTRACTING WITH BROKER
A. Elements Applicable to Both Sellers and Buyers
1. Essentials of Contract §2.43
2. Statute of Frauds
a. Contents of Required Writing §2.44
(1) Employment of Broker §2.45
(2) Identity of Property §2.46
(3) Execution of the Writing §2.47
b. No Compensation Without a Writing §2.48
c. Theories of Recovery in Absence of a Writing
(1) Quasi-Contract Theory §2.49
(2) Fraud and Misrepresentation §2.50
(3) Estoppel Theory §2.51
d. Exceptions §2.52
e. Modification of Listing Agreement §2.53
B. Seller-Broker Listing Agreements §2.54
1. Listing Agreement Checklist §2.55
2. Types of Listing Agreements
a. Exclusive Right to Sell
(1) General Characteristics §2.56
(2) Form: Residential Listing Agreement (Exclusive Authorization and Right to Sell) (CAR Form RLA) §2.57
b. Exclusive Agency §2.58
c. Open Listing
(1) General Characteristics §2.59
(2) Form: Nonexclusive ("Open") Agency Residential Listing Agreement (Authorization and Right to Sell) (CAR Form RLAN) §2.60
d. Net Listing Provisions §2.61
3. Forms and Provisions for Listing Agreements §2.62
a. Termination Date
(1) Need for Definite Date §2.63
(2) Form: Listing Period §2.64
b. Listing Price
(1) Negotiating Listing Price; Method of Payment §2.65
(2) Form: Listing Price §2.66
c. Buyer's Deposit
(1) Broker Holding Buyer's Deposit §2.67
(2) Form: Authority to Accept Deposits §2.68
(3) Handling Deposits §2.69
(4) Form: Handling Deposits §2.70
d. Escrow Holder
(1) Selection of Escrow Holder §2.71
(2) Form: Designating Escrow Holder §2.72
e. Form: Possession §2.73
f. Multiple Listing Services
(1) Use of MLS §2.74
(2) Form: Broker Cooperation; Submitting Listing to MLS §2.75
g. Broker's Compensation
(1) Conditioned on Closing §2.76
(2) Not Conditioned on Closing §2.77
(3) Payment From Deposits §2.78
(4) Form: Entitlement to Commission §2.79
(5) Form: Buyers Excluded From Agency §2.80
h. Safety Clauses
(1) Purpose of Safety Clause §2.81
(2) Form: Sale After Termination of Listing Agreement (Safety or Protection Clause) §2.82
i. Broker's Duties
(1) Duties Performed; Use of Due Diligence §2.83
(2) Form: Broker's Duties §2.84
j. Arbitration §2.85

k. Execution; Acknowledgment of Receipt
(1) Execution §2.86
(2) Form: Printed Form Subordinate to Drafted Provisions §2.87
(3) Form: Acknowledgment of Receipt; Broker's Acceptance §2.88
C. Buyer-Broker Agreements
1. General Considerations §2.89
2. Form: Buyer Representation Agreement—Exclusive (CAR Form BRE) §2.90

V. BROKER'S COMPENSATION
A. Prerequisites to Broker's Right to Commission §2.91
1. Listing (Seller's) Broker §2.92
2. Cooperating (Buyer's) Broker §2.93
3. License Required to Recover Compensation §2.94
4. Written Contract Required §2.95
5. Broker Must Not Represent Self §2.96
6. Contract Provisions Govern §2.97
7. Transactions Other Than Outright Sale §2.98
8. Procuring Cause
a. Definition §2.99
b. Factors to Consider
(1) Introduction of Parties §2.100
(2) Showing Property §2.101
(3) Completion of Sale §2.102
(4) Type of Listing Agreement §2.103
(5) Cooperating Broker §2.104
(6) Safety or Protection Clause §2.105
9. Ready, Willing, and Able Buyer
a. Basic Considerations §2.106
b. Offer Rejected by Seller §2.107
c. Offer Accepted: Sale Not Completed §2.108
d. Nonconforming or Conditional Offer Accepted §2.109
10. Conditional Commission Provision §2.110
a. Examples of Conditions §2.111
b. Provisions in Standard Forms
(1) Residential Exclusive Authorization and Right to Sell §2.112
(2) Real Estate Residential Purchase Agreement and Receipt for Deposit §2.113
B. Broker's Rights Under Withdrawal-From-Sale Clause §2.114
C. Sale After Listing Period
1. When Broker Can Recover Commission §2.115
2. Activity Required to Recover Under Safety Clause §2.116
3. Danger of Liability for Two Commissions §2.117
D. Amount of Commission §2.118
E. Buyer's Breach: Broker's Right to Deposit or Damages §2.119
F. Recovery of Commission From Buyer
1. Implied Covenant to Complete Purchase §2.120
2. Interference With Prospective Economic Advantage §2.121
a. Elements of Cause of Action §2.122
b. Problems of Proof §2.123

VI. BROKER'S FIDUCIARY DUTIES TO CLIENT
A. Standard of Care §2.124
1. Duty Arises When Agency Created §2.125
2. Duty May Survive Closing §2.126
B. Duty to Disclose §2.127
1. Conflicts of Interest §2.128
a. Dual Agency §2.129
b. Other Multiple Agency Scenarios §2.130
c. Self-Dealing §2.131
(1) Broker's Purchase of Client's Property: Disclosure Requirements §2.132
(2) Indirect Sales §2.133
(3) Broker's Interest in Property Sold to Client §2.134
d. Secret Profits §2.135
e. The Dishonest Client §2.136
2. Advice on Price and Value §2.137
a. Best Price Obtainable §2.138

b. Statements to Parties About Price §2.139
c. Speculative Purchases and Resales §2.140
d. Communicating Offers to Seller §2.141
C. Duty to Exercise Reasonable Care §2.142
1. Advice on Financial Soundness §2.143
2. Advice on Title Matters §2.144
3. Advice on Real Estate Matters §2.145
4. Advice on Tax Considerations §2.146
5. Advice on Legal Matters §2.147
6. Advice on Short Sales §2.147A
D. Duty to Perform With Diligence §2.148
E. Duty to Account §2.149
F. Limitations on Broker's Duties
1. No Duty to Verify Accuracy of Others' Representations §2.150
2. No Duty to Advise on Matters Outside of Broker's Expertise §2.151

VII. CLAIMS AGAINST BROKER
A. Breach of Fiduciary Duty §2.152
1. Bases of Liability §2.153
2. Pre-Litigation and Pre-Arbitration Duty to Mediate §2.153A
3. Right to Arbitrate Claims §2.154
4. Damages for Breach of Fiduciary Duty §2.155
a. Breach of Contract; Fraud Actions §2.156
b. Tort Action §2.157
c. Attorney Fees §2.158
B. Damages for Negligence §2.159
C. Recovery of Secret Profits §2.160
D. Recovery of Commission §2.161
E. Punitive Damages §2.162
F. Indemnity §2.163
G. Recovery of Unsatisfied Judgments From Recovery Account of Real Estate Fund §2.164
1. Requirements for Recovery
a. Licensed Defendant §2.165
b. Basis of Judgment §2.166
c. Specified Categories of Actions §2.167
d. No Discharge in Bankruptcy §2.168
2. Amounts Recoverable §2.169
3. Procedures §2.170

VIII. DISCIPLINARY PROCEEDINGS
A. Real Estate Commissioner Proceedings
1. Grounds for Imposing Discipline §2.171
2. Procedures and Remedies
a. Mitigating Factors §2.172
b. Disciplinary Proceedings §2.173
c. Remedies §2.174
B. Local Association of Realtors® Proceedings §2.175

IX. BROKER LIABILITY TO THIRD PARTIES §2.176
A. Secret Profits §2.177
B. Fraud, Misrepresentation, and Failure to Disclose §2.178
C. Negligence §2.179
D. Breach of Contract §2.180
E. Housing Discrimination §2.181
F. Anti-Money-Laundering Laws §2.182
G. Principal to Broker; Indemnification §2.183

X. PRINCIPAL LIABLE TO THIRD PARTIES FOR BROKER'S ACTS
A. Misrepresentations and Nondisclosure §2.184
B. Effect of Exculpatory "As Is" Provision §2.185
C. Broker's Failure to Disclose Principal §2.186
D. Liability to Subsequent Purchasers §2.187

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.1 I. REGULATION OF BROKERS

§2.1 I. REGULATION OF BROKERS

In California, the real estate brokerage industry is regulated by statute (Bus & P C §§10000-10580, commonly known as the Real Estate Law) and by administrative regulations adopted by the Real Estate Commissioner (10 Cal Code Regs §§2705-3109). This discussion of the regulatory scheme briefly addresses the following topics:

- Broker's licensing requirements and who must obtain a license (§§2.2-2.5);
- Exemptions from the licensing regulations (§2.6);
- Types of specialized licenses (§§2.7-2.11);
- Broker's advertising regulations (§2.12);
- The broker's relationship with the salespersons (§§2.13-2.21); and
- The broker as escrow agent (§§2.22-2.23).

For an in-depth treatment of brokers, including regulation and discipline, see California Real Estate Brokers: Law and Litigation (Cal CEB 2009).

© The Regents of the University of California

§2.2 A. Licensing

It is unlawful for anyone to act as a real estate broker or salesperson without first obtaining a license from the Department of Real Estate (DRE). Bus & P C §10130. For more information about the DRE, see the DRE website listed in the Directory.

According to the licensing provisions of the Real Estate Law, a real estate broker is someone who performs specified acts for another person and for compensation. Among other things, a broker:

- Sells or offers to sell, or buys or offers to buy, real property (Bus & P C §10131(a));
- Solicits prospective sellers or buyers, solicits or obtains listings, or negotiates for the purchase, sale, or exchange of real property or a business opportunity (Bus & P C §10131(a));
- Charges an advance fee in connection with various specified activities relating to the sale or lease of real property (Bus & P C §10131.2);
- Collects payments or performs other services for borrowers, lenders, or note owners in connection with loans secured by liens on real property (Bus & P C §10131(d); see also §2.7 on loan brokering activities and Bus & P C §10133.1(b) for certain exemptions on collection of loan payments);
- Sells or offers to sell, buys or offers to buy, or exchanges or offers to exchange real property sales contracts or promissory notes secured by a lien on real property, as either an agent or the principal (Bus & P C §§10131(e), 10131.1);
- Sells or exchanges with the public eight or more real property sales contracts or promissory notes secured directly or collaterally by liens on real property during one calendar year (Bus & P C §10131.1(b)(1)(B)); or
- Makes eight or more loans in a calendar year from the broker's own funds to the public when those loans are held or resold and secured directly or collaterally by residential real property (Bus & P C §10131.1(b)(1)(C)).

For a complete list of activities requiring a real estate broker's license, see Bus & P C §10131.

An individual convicted of acting as a real estate broker or a real estate salesperson without a license is punishable by a fine not to exceed $20,000 or by imprisonment for a term not to exceed 6 months, or both. A convicted corporation is punishable by a fine not to exceed $60,000. Bus & P C §10139.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.3 1. Licensing Qualifications

§2.3 1. Licensing Qualifications

To obtain a real estate license, brokers and salespersons must pass a written examination. Bus & P C §10153. Applicants must also meet the experience requirements in Bus & P C §10150.6 and the educational requirements in Bus & P C §§10153.2, 10153.3-10153.5. The Commissioner may deny a license if the applicant is dishonest. Bus & P C §10177(j). See *Harrington v Department of Real Estate* (1989) 214 CA3d 394, 263 CR 528 (contracting without license and passing worthless check are crimes of moral turpitude justifying denial of license).

NOTE: California attorneys (members of the State Bar) are exempt from the educational requirements for a real estate salesperson license. Bus & P C §10151(d).

© The Regents of the University of California

§2.4 2. Corporations and Partners as Licensees

A corporation can be licensed as a real estate broker, and the corporate license entitles one designated officer (who individually holds a broker's license) to act as a broker on behalf of the corporation without payment of any further licensing fee. Bus & P C §10211. If more than one officer of a corporation acts as a broker, the corporation must obtain additional licenses for each of them (Bus & P C §10158), and each officer through whom the corporation acts as a licensee must pass the DRE's written examination (Bus & P C §10153). Acts for which a real estate license is required may be conducted by the corporation only if there is an officer licensed under Bus & P C §10158 or §10211. 10 Cal Code Regs §2740.

A corporation's real estate broker's license cannot be revoked for violation of the Real Estate Law if the violating broker had completely disassociated himself from the corporation at the time of revocation. *Amvest Mortgage Corp. v Antt* (1997) 58 CA4th 1239, 68 CR2d 457. Clarifying legislation provides that the DRE may still discipline the corporation or deny it a license, even if the violator has disassociated from the corporation, if the offending officer, director, or stockholder violated the Real Estate Law while acting on behalf of the corporate broker. Bus & P C §10177(p).

Although there is no provision for a broker's license to be issued to a partnership, individual licensed brokers can form a partnership. Bus & P C §10137.1. A salesperson can act on behalf of a partnership if the employing broker is a partner. 10 Cal Code Regs §2755. A partnership consisting of both licensees and nonlicensees may act as a broker as long as the partners through whom it acts are licensed. Bus & P C §10137.1. A broker's license may be issued in a fictitious name as long as the broker has registered the fictitious name with the DRE. Bus & P C §10159.5.

© The Regents of the University of California

§2.5 3. Brokers Distinguished From Finders

California courts have long distinguished between a person acting as a real estate broker and a person acting merely as a "finder" and have ruled that a finder is not subject to the licensing requirements of the Real Estate Law. The terms "finder" and "middleman" are used interchangeably to refer to one whose role in a transaction is limited to introducing the principals, leaving it to them to negotiate the terms of their contract. *Tyrone v Kelley* (1973) 9 C3d 1, 106 CR 761. In contrast, a broker actually plays a role in bringing about a meeting of the minds between the parties. *Eaton v Yount* (1920) 48 CA 221, 191 P 1009. An intermediary who engages in any activity beyond merely arranging an introduction of seller and buyer will be classified as engaging in an activity requiring a license as a broker. *Zappas v King Williams Press, Inc.* (1970) 10 CA3d 768, 89 CR 307.

A person acting as a finder without having a broker's license will be able to recover a fee (*Tenzer v Superscope, Inc.* (1985) 39 C3d 18, 216 CR 130), but a person acting as a broker without a license will not (*Hasekian v Krotz* (1968) 268 CA2d 311, 74 CR 410). A lawyer, not licensed as a real estate broker, who engages in licensed activities, however, is not protected by the finder's exception. *Preach v Monter Rainbow* (1993) 12 CA4th 1441, 16 CR2d 320. See §2.94 on a license as a prerequisite to compensation.

The distinction between broker and finder is important not only because a finder need not be licensed, but also because a finder does not owe the same fiduciary duty to the principal that a broker does. *Batson v Strehlow* (1968) 68 C2d 662, 68 CR 589. See §§2.124-2.187 for discussion of brokers' fiduciary and other duties. Because a finder has no fiduciary obligations, courts are reluctant to find that an intermediary is merely a finder. *Batson v Strehlow, supra*.

PRACTICE TIP: As a practical matter, an intermediary's activities are rarely limited to those of a mere finder, especially in large commercial transactions. An intermediary who expects compensation on consummation of the transaction will likely want to be involved in the negotiation and performance of the contract in an effort to ensure completion of the transaction, rather than leaving the entire process in the hands of the principals. In such circumstances the intermediary should also expect to be considered a broker rather than a finder.

An intermediary's ability to collect a finder's fee is further restricted by the Real Estate Settlement Procedures Act of 1974 (RESPA) (12 USC §§2601-2617; 24 CFR §§3500.1-3500.21). Referral fees and fee-splitting arrangements are barred in transactions involving four or fewer dwelling units that are financed by loans secured by first deeds of trust obtained from federally insured lending institutions. 12 USC §§2602, 2607; 24 CFR §3500.14. Fees for services actually performed, "affiliated business arrangements" (as long as certain advance notices are given to the person being referred), and payments under cooperative broker and referral arrangements or agreements between real estate agents and brokers are all exempt from this prohibition. See 12 USC §2607(c); 24 CFR §§3500.14(g)(1), 3500.15. The latter exemption has yet to be interpreted by the courts, and it is unclear whether it exempts any finder's fee paid to a licensed broker or exempts only referrals between brokers in different geographical areas. See 2 Miller & Starr, California Real Estate §§4:29, 5:3, 36:26 (3d ed 2000). See chap 15 for further discussion of RESPA. Under California law, real estate agents are prohibited from receiving a "commission, fee, or other consideration" for referral of clients to an "escrow agent, structural pest control firm, home protection company, title insurer, controlled escrow company, or underwritten title company," unless such compensation falls within an exception provided by the statute. See Bus & P C §10177.4.

For restrictions on title companies, see Ins C §§12404-12413.5.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.6 4. Exemptions From Licensing Requirements

§2.6 4. Exemptions From Licensing Requirements

Generally, a broker's license is required only for activities undertaken on behalf of others. Bus & P C §§10131, 10133(a). See, *e.g., Robinson v Murphy* (1979) 96 CA3d 763, 158 CR 246. Persons who perform any of the activities described in §§2.2 and 2.7-2.11 with respect to their own property are exempt from the licensing requirements of the Real Estate Law. A few specifically enumerated activities, however, require a license even when the individual is acting as the principal. For example, a person who engages as a principal in the business of buying, selling, or exchanging real property sale contracts or notes secured by liens on real property must be licensed as a broker. Bus & P C §10131.1; see §2.2.

The Real Estate Law also provides the following exemptions:

- Certain types of individuals are exempt from licensing requirements (for a complete list see Bus & P C §10133); and
- Certain entities and companies are exempt from broker licensing requirements in connection with their activities in making, negotiating, or arranging mortgage loans, or in purchasing, servicing, and selling promissory notes secured by real property (for a complete list of these exemptions, see Bus & P C §10133.1).

© The Regents of the University of California

B. Specialized Licensees

§2.7 1. Mortgage Loan Brokers

A real estate broker's license is required for anyone who solicits borrowers or lenders for, or negotiates loans secured directly or collaterally by, liens on real property. Bus & P C §10131(d). A broker's employee assisting the broker in residential mortgage loan transactions may be exempt from the license requirement. See §2.6.

A real estate license endorsement is required to engage in the business of a mortgage loan originator. Fin C §22100. In addition, mortgage loan brokers' activities are regulated under both the Real Property Loan Law (Bus & P C §§10240-10248.3) and regulations adopted by the Real Estate Commissioner (10 Cal Code Regs §§2840-2849.01). Specifically, the license endorsement requirement entails education, written testing, and reporting duties. The requirement comports with the creation of a Nationwide Mortgage Licensing System and Registry (NMLS) under the federal Secure and Fair Enforcement Mortgage Licensing Act of 2008 (SAFE) (12 USC 5101-5116). Finance lenders and residential mortgage lenders under the Department of Corporation must register in the nationwide system by July 1, 2010. Real estate brokers who originate mortgages must comply by December 1, 2010. In addition, if a real estate broker or the broker's salesperson makes, arranges, or services loans secured by residential property containing 1-4 units, the broker must notify the DRE by January 31, 2010 or within 30 days of commencing such loan activity, whichever is later.

© The Regents of the University of California

§2.8 a. Disclosure Requirements and Limits on Charges

A mortgage loan broker owes a fiduciary duty to the borrower, including a duty to point out to an unsophisticated borrower any unfavorable loan provisions. *Wyatt v Union Mortgage Co.* (1979) 24 C3d 773, 157 CR 392 (broker failed to disclose unfavorable terms regarding interest, late charges, and size of balloon payment; borrowers were awarded punitive damages for breach of broker's duty). In *Realty Projects, Inc. v Smith* (1973) 32 CA3d 204, 108 CR 71, the borrowers sought loans within the coverage of the Real Property Loan Law (Bus & P C §§10240-10248.3) but were persuaded by the broker to borrow above the applicable regulated loan limit. The court, in sustaining an order suspending and revoking the brokers' real estate licenses, held that they were required to disclose to the borrowers that the commissions and other charges would have been substantially lower if the loans had been within the coverage of Bus & P C §10245.

The Real Property Loan Law protects borrowers by limiting the fees that may be charged on regulated loans and by requiring detailed and specific disclosure of loan charges. The law applies generally to loans secured by real property that are made or negotiated by a real estate broker. Bus & P C §§10240(b), 10248.3. For maximum charges that can be imposed for brokerage costs and expenses, including appraisal fees, escrow, title, notary, recording, and credit investigation fees (but exclusive of title and recording charges) in a mortgage loan subject to the Real Property Loan Law, see Bus & P C §10242(a).

The law also requires the broker to give the borrower a detailed mortgage loan disclosure statement in the form prescribed by the DRE that discloses, among other things, the amount of commissions and all other costs charged to the borrower. Bus & P C §§10240-10241; 10 Cal Code Regs §2840 (approved borrower disclosure statements). For a federally regulated residential mortgage loan of $30,000 or more in principal and secured by a first deed of trust (or $20,000 or more and secured by a junior deed of trust), the broker's disclosure obligations are satisfied if (1) the borrower receives a "good faith estimate" that satisfies the Real Estate Settlement Procedures Act of 1974 (RESPA) (12 USC §§2601-2617) and that includes the broker's license number and a statement that it is not a loan commitment; (2) the borrower receives applicable disclosures required by the Truth in Lending Act (15 USC §§1601-1693r); and (3) if the loan provides for a balloon payment, the loan contains a balloon payment disclosure meeting specified standards. Bus & P C §§10240(c), 10245. Generally, the "good faith estimates" are satisfied when the buyer receives the Estimated and Final Closing Statements from the escrow or title company.

The broker must retain a copy of the disclosure documentation, as acknowledged by the borrower, for a period of 3 years. Bus & P C §10240(a), (c). This requirement applies to all loans made or arranged by real estate brokers, not only those secured by a dwelling. Bus & P C §§10240.1, 10248.3. On disclosure and compliance requirements for nontraditional and subprime mortgage products, see §2.8A-2.8B.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.8A b. Disclosure and Compliance Requirements for Nontraditional and Subprime Mortgage Products

§2.8A b. Disclosure and Compliance Requirements for Nontraditional and Subprime Mortgage Products

On January 14, 2008, in response to concerns regarding nontraditional and subprime mortgage products, emergency regulations were added to the law regarding mortgage disclosures. 10 Cal Code Regs §2844. The new regulations specify strict, minimum-risk management practices, underwriting standards, control systems, and consumer protection to which brokers must adhere. 10 Cal Code Regs §2844.

Among other things, the broker must consider the borrower's ability to repay a mortgage loan according to its terms as the primary basis for making a loan rather than the foreclosure or liquidation value of the collateral. 10 Cal Code Regs §2844(b)(1)(A). In analyzing repayment capacity, the broker must include an evaluation of the borrower's ability to repay the loan by final maturity at the fully indexed rate, assuming a fully amortized repayment schedule. 10 Cal Code Regs §2844(b)(2)(A).

The broker must avoid combining nontraditional loan features such as interest-only or negative amortization loans with reduced documentation or simultaneous second-lien loans absent specific mitigating factors such as high credit scores and low loan-to-value ratios. 10 Cal Code Regs §2844(b)(2)(B). When making loans categorized as subprime, the broker must ensure that such programs do not feature terms that could become predatory or abusive as described in certain specified guides and publications. 10 Cal Code Regs §2844(b)(2)(E).

Brokers must design compensation programs that avoid providing incentives for originations inconsistent with sound underwriting and consumer protection principles (10 Cal Code Regs §2844(b)(3)(A)) and monitor the quality of third party originations so that they reflect the broker's lending standards and compliance with the Real Estate Law (Bus & P C §§10000-10580) (10 Cal Code Regs §2844(b)(3)(B)).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.8B c. SB 94 and AB 260

§2.8B c. SB 94 and AB 260

In October 2009 the California legislature adopted AB 260 (2009) and SB 94 (2009) in response to the mortgage crisis of the late 2000s and the resultant growth in loan modification and foreclosure rescue scams. The provisions of AB 260 do not go into effect until January 1, 2010, but SB 94 was adopted as an urgency measure, and thus goes into effect immediately.

WARNING: Both AB 260 and SB 94 amend Bus & P C §10177 with slightly different effect (SB 94 adds subsection (q), while AB 260 adds subsections (q) and (r), discussed below). Both bills were chaptered on October 11, 2009, with AB 260 as Chapter 629 and SB 94 as Chapter 630. The normal rule is that the later chaptered bill controls. Govt C §9605. Here, however, the later chaptered bill is an urgency measure, going into effect immediately and the earlier chaptered bill does not go into effect for several months. Did the legislature intend that changes to the statute in the earlier bill would amend the changes made by the later bill? It appears to do just that, but is not addressed in the discussion of the bills provided by the legislative counsel. The situation will resolve itself in January 2010 when SB 260 goes into effect.

Senate Bill 94 immediately amends several existing statutes and adds a number of new statutes applicable to loan modifications involving 1-4 residential units. Senate Bill 94 does not apply to actions taken by a person offering loan modifications on loans owned or serviced by that person. The provisions of SB 94 sunset on January 1, 2013, unless extended, and include the following changes:

- New Bus & P C §10147.6 requires brokers involved in residential loan modifications to provide clients with a disclosure notice stating that it is not necessary to pay a third party for loan modification services and that such services are available for free from the U.S. Department of Housing and Urban Development. New CC §2944.6 requires anyone involved in residential loan modifications to provide such notice. The notice must be in 14-point bold type and in the language in which the loan modification is offered or negotiated. Penalties for noncompliance include fines of up to $50,000 for entities and $10,000 and/or 1 year imprisonment in county jail for individuals.
- New Bus & P C §10085.6 prohibits brokers involved in residential loan modifications from collecting "advance fees" or a power of attorney from clients. New CC §2944.7 prohibits anyone from collecting such fees or obtaining a power of attorney from clients. Penalties for violating these statutes include fines of up to $50,000 for entities and $10,000 and/or 1 year imprisonment in county jail for individuals.
- New subsection Bus & P C §10177(q) provides that the Real Estate Commissioner may suspend or revoke the license of a broker, or may deny the issuance of a license to an applicant, who has violated or failed to comply with CC §§2920-2944.7.
- New Bus & P C §6106.3 provides that attorneys violating new CC §§2944.6-2944.7 are subject to discipline procedures.
- New Bus & P C §10026 redefines "advance fee" as a fee collected before completion of each and every service a broker has contracted to perform.
- New Bus & P C §10085 requires brokers to submit certain documents pertaining to advance fees to the Real Estate Commissioner at least 10 calendar days before use and imposes fines of up to $2500 and misdemeanor penalties for noncompliance.
- New subsection Bus & P C §10133.1(11) provides that as to any organization or employee of an organization approved by the U.S. Department of Housing and Urban Development to provide free residential loan modification counseling services, such persons:
- are not "real estate brokers" within the meaning of Bus & P C §10131 and 10131.1.
- are not subject to CC §1695.13 prohibiting unconscionability in residential real property foreclosures.
- are exempt from regulation of mortgage loan brokers' activities under the Real Property Loan Law (Bus & P C §§10240-10248.3).
- New definitions in existing CC §2945.1 cover, among other things, "foreclosure consultant" and "residence in

foreclosure."

- New Fin C §22161(a) prohibits any person from making a materially false or misleading statement or representation to a borrower about the terms or conditions of the borrower's loan when making or brokering the loan.

Assembly Bill 260 goes into effect on January 1, 2010 and includes the following changes relevant to brokers:

- New subsection Bus & P C §10177(q) provides that the Real Estate Commissioner may suspend or revoke the license of a broker, or may deny the issuance of a license to any applicant, who violates the provisions of the Real Estate Settlement Procedures Act of 1974 (RESPA) (12 USC §§2601-2617; 24 CFR §§3500.1-3500.21), the Truth in Lending Act (TILA) (15 USC §§1601-1693r), the Home Ownership Equity Protection Act (15 USC §1639), or any of the regulations promulgated under these federal acts.
- New subsection Bus & P C §10177(r) provides that the Real Estate Commissioner may suspend or revoke the license of a broker, or may deny the issuance of a license to any applicant, who has violated or failed to comply with CC §§2920-2944.7.
- New CC §2923.1 provides that a mortgage broker is a fiduciary of its borrower-client and defines "mortgage broker" as a licensed real estate broker who provides mortgage brokerage services. Any violation of the broker's fiduciary duties is a violation of mortgage broker's licensing law and incurs requisite civil penalties and liability. The mortgage broker's fiduciary duty to its client includes a duty to place the economic interest of the client ahead of the economic interest of the broker.
- New Fin C §§4995-4995.6 affects certain loans originated on or after July 1, 2010 and establishes a category of residential loans defined as "higher-priced mortgage loans"; prohibits brokers and others from making false, deceptive, or misleading statements or representations in connection with such loans; restricts broker compensation received on such loans containing prepayment penalties to certain limits; and provides that any violation of these statutes by a broker is punishable by civil penalty of up to $10,000.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.9 d. Exemption From Usury for Loans Made or Arranged by Broker

§2.9 d. Exemption From Usury for Loans Made or Arranged by Broker

A loan secured by real property and made or arranged by a real estate broker is exempt from usury limitations. Cal Const art XV, §1. This exemption was given retroactive effect in *Chapman v Farr* (1982) 132 CA3d 1021, 183 CR 606, thus protecting brokers from liability for usury in transactions that occurred before the enactment of the constitutional amendment. Lind, *A Real Estate Attorney's Guide to California Usury Laws*, 18 CEB Real Prop L Rep 271 (Oct 1995). See Harroch & Dana, *The Real Estate Broker Exemption From the California Usury Law*, 4 CEB Real Prop L Rep 137 (Nov. 1981).

The phrase "make or arrange" does not include a loan in which the broker was a borrower; it includes only loans in which the broker is either a lender or a third party acting for others for compensation. *Winnett v Roberts* (1986) 179 CA3d 909, 225 CR 82; CC §1916.1. However, the exemption does apply when the borrower is a limited partnership and the loan is arranged by a broker who acts in the capacity of general partner. A loan arranged by a broker acting in his capacity as the general partner of a borrower that is a limited partnership, however, does qualify for the exemption. See *Park Terrace Ltd. v Teasdale* (2002) 100 CA4th 802, 807, 122 CR2d 797;see also *Stickel v Harris* (1987) 196 CA3d 575, 242 CR 88 (broker did not lose exempt status by joining borrowing joint venture). The expected compensation may be the right to participate in the borrowing entity's anticipated profits. See *Park Terrace Ltd. v Teasdale, supra*.

Civil Code §1916.1 restricts the foregoing usury exemption to situations in which the broker:

- Acts for compensation or in expectation of compensation for soliciting, negotiating, or arranging the loan for another;
- Acts for compensation or in expectation of compensation for selling, buying, leasing, exchanging, or negotiating the sale, purchase, lease, or exchange of real property or a business for another and (1) arranges a loan to pay all or any portion of the purchase price of, or of an improvement to, that property or business, or (2) arranges a forbearance, extension, or refinancing of any loan in connection with that sale, purchase, lease, exchange of, or improvement to, real property or a business; or
- Arranges or negotiates for another a forbearance, extension, or refinancing of any loan secured by real property in connection with a past transaction in which the broker had acted for compensation or in expectation of compensation for selling, buying, leasing, exchanging, or negotiating the sale, purchase, lease, or exchange of real property or a business.

NOTE: The actions of simply preparing loan documents according to instructions and on terms provided by the parties, ordering title insurance, and dispersing funds do not constitute "arranging" a loan under Cal Const art XV, §1, or under CC §1916.1 See *Gibbo v Berger* (2004) 123 CA4th 396, 402, 19 CR3d 829 ("When viewed in the context of 'arranging a loan,' the phrase 'arranged by' must refer to some conduct by a real estate broker, acting as a third party intermediary rather than as a party to the loan, that causes a loan to be obtained or procured").

On the broker's duty to disclose the fact that it is arranging a loan, see §2.31.

© The Regents of the University of California

§2.10 2. Business Opportunity Brokers

A business opportunity broker is required to be licensed as a real estate broker. Bus & P C §10131. As defined in the Real Estate Law, the term "business opportunity" includes "the sale or lease of the business and goodwill of an existing business enterprise or opportunity." Bus & P C §10030. A sale of all or substantially all assets of a corporation, partnership, or sole proprietorship is considered a business opportunity, and the sale of all or substantially all the shares of a corporation may also be considered a business opportunity. *All Points Traders, Inc. v Barrington Assocs.* (1989) 211 CA3d 723, 259 CR 780. Licensed security broker-dealers, however, can broker the sale of a business opportunity without a real estate license. Bus & P C §10008.5.

© The Regents of the University of California

§2.11 3. Real Estate Syndicate Securities Dealers

Real estate syndications may take many forms, but they are generally a means of pooling investors' funds for investment in real estate. They are most often formed to purchase, develop, or construct real property or to make loans secured by real property. Most syndications involve the offer and sale of a security within the meaning of California's Corporate Securities Law of 1968 (Corp C §§25000-25707) and the federal Securities Act of 1933 (15 USC §§77a-77aa). For example, limited partnership interests, investment contracts, interests in an unincorporated association such as a trust, and multiple interests in promissory notes constitute securities. Corp C §25019 (definition of securities). See also *People v Woodson* (1947) 78 CA2d 132, 177 P2d 586 (limited partnership interests are securities). Anyone who offers or sells securities as a principal or a broker must generally be licensed as a "broker-dealer" by the Department of Corporations. Corp C §25210. For exemptions from the broker-dealer licensing requirement, see Corp C §25206; Bus & P C §10131.3.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.12 C. Real Estate Advertising

§2.12 C. Real Estate Advertising

Under California law, real estate brokers who advertise services for which a license is required must use terms such as "broker," "bro.," "agent," "agt.," "licensee," or "Realtor®" to indicate advertising by a real estate licensee, and the name of the broker. Bus & P C §§10140.5-10140.6; 10 Cal Code Regs §2770.1. The broker must supervise all activities, including the advertisements of its agents. See 10 Cal Code Regs §2725(e). Loan advertising has additional requirements. See Bus & P C §§10235.5, 17539.4. See also Bus & P C §10236.4 (requiring broker's license number on certain advertisements).

Advertisements must not be false or misleading. Bus & P C §§10140, 17500. The DRE has not issued general guidelines for what constitutes false and misleading advertising in all cases.

For authority on the following subjects, refer to the regulation or code cited:

- Subdivision interests: 10 Cal Code Regs §2799.1;
- Mortgage loans: 10 Cal Code Regs §2848;
- Civil/criminal penalties for violation: Bus & P C §§17500, 17536(a);
- Internet advertisement laws: Bus & P C §§17500, 17530; 10 Cal Code Regs §2770;
- E-mail and facsimiles: Bus & P C §§17538.43, 17538.45; 47 USC §227; 47 CFR §68.318(d); and
- Telephones and autodialers: Bus & P C §§17511-17511.13; Pub Util C §§2871-2876; CC §1770(a)(22); 47 USC §227.

© The Regents of the University of California

§2.12A D. Interpretive Opinions

Brokers and attorneys seeking guidance regarding specific regulatory statutes or rules (*e.g.*, loan advertising, see §2.12) may request an interpretive opinion under Bus & P C §10236 by writing to the Department of Real Estate at the address set forth in the Directory. 10 Cal Code Regs §2845. Attorneys writing are requested to provide their own analysis of the issues presented along with citations to legal authority in support of any views expressed. 10 Cal Code Regs §2845.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/ E. Broker's Relationship With Salespersons/§2.13 1. Salesperson Licensing and Employment Requirements

E. Broker's Relationship With Salespersons

§2.13 1. Salesperson Licensing and Employment Requirements

A natural person employed by a licensed real estate broker to perform any act that requires a broker's license is a salesperson. See Bus & P C §10132 (definition of "real estate salesman"). A salesperson can be employed only by a licensed broker and cannot deal with the public except through that broker. Bus & P C §§10132, 10137; *Grand v Griesinger* (1958) 160 CA2d 397, 406, 325 P2d 475. A broker cannot employ a person who is not a licensed broker or a licensed salesperson to perform acts that require a license. Bus & P C §10137. A salesperson cannot be employed by, or accept compensation from, anyone other than the broker under whom he or she is currently licensed. Bus & P C §10137; *Hoar v Tuley* (1970) 12 CA3d 344, 348, 90 CR 559.

PRACTICE TIP: It is accepted DRE policy that the employing broker can pay its agent's commission through escrow as long as the broker has given written instructions to the escrow holder on a "transaction-by-transaction" basis.

© The Regents of the University of California

§2.14 2. Supervision of Salespersons

The statutory scheme of the Real Estate Law requires that a salesperson act only through and on behalf of a broker. Bus & P C §§10132, 10137, 10160. Similarly, a broker is required to supervise his or her salespersons and is subject to disciplinary action by the Real Estate Commissioner for failure to do so. Bus & P C §10177(h). The duty of supervision requires the broker to establish policies, rules, procedures, and systems to manage and review certain activities, including transactions for which a license is required, documents that may have a material effect on the rights or obligations of a party to the transaction, handling of trust funds, and advertising. 10 Cal Code Regs §2725.

© The Regents of the University of California

§2.15 a. Relationship Between Broker and Salesperson Under Bus & P C §10032

A salesperson may be either an independent contractor or an employee of the broker. Under Bus & P C §10032, the nature of the relationship—and the mutual legal obligations of the broker and salesperson—can vary with the relevant legal context or issue, *e.g.,* liability. The parties' characterization of the relationship is not determinative. *Brown v IAC* (1917) 174 C 457, 163 P 664; *Anderson v Badger* (1948) 84 CA2d 736, 191 P2d 768. For some purposes, such as withholding taxes, unemployment compensation, and workers' compensation, the character of the relationship may be governed by statutes other than §10032 (see §§2.17-2.19).

For purposes of liability to third parties, salespersons are generally considered employees of the broker. The broker's failure to properly supervise a salesperson can result in both (1) a civil judgment against the broker on a theory of vicarious liability arising from the salesperson's fraud, misrepresentation, or deceit, and (2) loss of the broker's license. Bus & P C §10177.5; CC §2079.13(b). This aspect of broker liability cannot be changed by contract or by characterizing the salesperson as an independent contractor. *Gipson v Davis Realty Co.* (1963) 215 CA2d 190, 30 CR 253. Furthermore, as demonstrated in *California Real Estate Loans, Inc. v Wallace* (1993) 18 CA4th 1575, 23 CR2d 462, the revocation of a broker's license under §10177.5 does not require any guilty knowledge on the broker's part, only the fact of a judgment against the broker. Administrative discipline against the broker who suffers a judgment based on a salesperson's misconduct provides a powerful incentive to guard against misconduct by salespersons in the future.

A supervising broker who also holds an ownership interest in a brokerage may be liable as a matter of law, under DRE regulations as well as traditional corporate vicarious liability law, for tortious acts committed by those salespersons working under the broker's supervision. *Holley v Crank* (9th Cir 2004) 400 F3d 667 (designated officer and broker of real estate company can be held personally liable for actions of employee and can be held liable through piercing company's corporate veil; but note that the opinion deletes language previously included in a predecessor opinion (*Holley v Crank* (9th Cir 2004) 386 F3d 1248) imposing liability for negligent supervision). See also *California Real Estate Loans, Inc. v Wallace, supra*; Bus & P C §10032; CC §2079.13(b).

© The Regents of the University of California

§2.16 b. Relationship Between Broker and Salesperson Under Common Law and Other Statutory Schemes

In contexts not specifically addressed in Bus & P C §10032, the character of the relationship between broker and salesperson generally will depend on the application of common law principles to the facts of a particular case. Under common law, the most important test of whether the relationship is that of employee or independent contractor is the degree to which the broker has the right to control the manner and means in which the salesperson's work is done. If the broker controls only the results to be achieved, the salesperson is likely an independent contractor. If the broker has the right to control the details of how services are performed (whether or not control is actually exercised), then the salesperson is likely an employee. See *Baugh v Rogers* (1944) 24 C2d 200, 148 P2d 633.

In addition to the common law test, the relationship between broker and salesperson must be considered in view of the legal context in which the inquiry arises, *i.e.,* the purposes intended by the applicable statutory scheme. Absent an overriding public policy or the clearly expressed intent of another statutory scheme, the duty to supervise imposed by the Real Estate Law historically has been interpreted to favor a finding of an employee-employer relationship.

© The Regents of the University of California

§2.17 c. Unemployment Insurance

Brokers and real estate salespersons are excluded from the coverage under California's unemployment insurance system under specified conditions; in particular, brokers must be licensed and salespersons must be independent contractors. See Un Ins C §650. If a salesperson is paid a salary, coverage turns on whether he or she is an independent contractor or an employee under Un Ins C §601, and this determination depends on the degree of control the broker is able to exercise. See, *e.g., Grant v Woods* (1977) 71 CA3d 647, 139 CR 533 (primary factor considered in determining whether employment relationship exists is where right of control lies within relationship). To obtain helpful information and publications on this topic, see the California Employment Development Department's website, listed in the Directory.

© The Regents of the University of California

§2.18 d. Worker's Compensation

The status of a real estate salesperson under the California Workers' Compensation Act (Lab C §§3200-6208) remains a question of fact to be analyzed on a case-by-case basis, as governed by the definitions of "employee" and "independent contractor" set forth in the Act. Lab C §§3350-3351, 3353. The common law test for employees—the right of control over the means of performing services—applies in this context. *Flickenger v IAC* (1919) 181 C 425, 184 P 851; *Esquer v Teresi* (1951) 105 CA2d 89, 232 P2d 895. In the cases decided before the enactment of Bus & P C §10177 (on suspension and revocation of licenses), the results were mixed. For cases discussing whether a salesperson qualified as an employee for workers' compensation purposes, see *Brown v IAC* (1917) 174 C 457, 163 P 664 (salesman deemed employee); *Cameron v Pillsbury* (1916) 173 C 83, 159 P 149 (real estate manager was employee); *Payne v White House Props., Inc.* (1980) 112 CA3d 465, 169 CR 373 (salesperson was not employee); *Royal Indem. Co. v IAC* (1930) 104 CA 290, 285 P 912 (agent was employee); *Hartford Acc. & Indem. Co v IAC* (1928) 93 CA 313, 269 P 733 (salesperson was employee).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.19 e. Withholding Income and Social Security Taxes

§2.19 e. Withholding Income and Social Security Taxes

Income, employment, and social security taxes must be withheld from compensation paid to employees, but those taxes cannot be withheld from independent contractors. IRC §§3102(a), 3401-3403, 3501-3510. Moreover, real estate salespersons receive specific statutory treatment. A licensed salesperson will not be considered an employee if (1) compensation is based on sales or other output rather than number of hours worked, and (2) the salesperson and the broker have a written contract that states that the salesperson will not be treated as an employee for withholding purposes. IRC §3508(b). California has a similar statutory exemption from state withholding requirements. Un Ins C §13004.1. If the salesperson does not satisfy its specific requirements, however, the control test must be used to determine whether the salesperson is an employee or an independent contractor.

© The Regents of the University of California

§2.20 f. Tort Liability

For purposes of the Real Estate Law, salespersons are agents of their brokers as a matter of law. *Gipson v Davis Realty Co.* (1963) 215 CA2d 190, 30 CR 253; see §2.14. Under both common law principles of agency and statutory law, brokers are liable as a matter of law for the torts committed by their salespersons within the course and scope of their agency. *California Real Estate Loans, Inc. v Wallace* (1993) 18 CA4th 1575, 23 CR2d 462; Bus & P C §10032; CC §2079.13(b). This is true even if the salesperson is otherwise classified as an employee or independent contractor. An employer is required by statute to indemnify an employee for all expenses or losses necessarily incurred in the performance of his or her job or while obeying the directions of the employer, whether or not lawful, unless the employee believed the acts to be unlawful at the time the directions were obeyed. Lab C §2802(a). Any contract made by an employee that purports to waive this right is null and void. Lab C §2804. Although independent contractors are not entitled to indemnification under §2802, a real estate salesperson who is an employee of a broker should be indemnified for any tort liability necessarily arising from services performed in the scope of employment. Independent contractor agreements with real estate salespersons commonly allocate defense costs (and sometimes judgments and settlements) between the broker and the salesperson.

© The Regents of the University of California

§2.21 3. Documenting Relationship Between Broker and Salesperson

A broker must have a written agreement with each salesperson, whether licensed as a salesperson or as a broker. 10 Cal Code Regs §2726. The agreement must set forth the material terms of the agreement, including supervision of licensed activities, duties, and compensation. 10 Cal Code Regs §2726. The broker must notify the DRE within 5 days of a broker's employment of a salesperson or of another broker. Bus & P C §10161.8; 10 Cal Code Regs §2752. A salesperson cannot accept compensation from anyone except the broker under whom the salesperson is licensed at the time. The salesperson's right to compensation is based solely on the agreement with the broker. Bus & P C §10137.

© The Regents of the University of California

F. Broker as Escrow Agent

§2.22 1. License Requirements

Escrow agents are regulated by California's Escrow Law (Fin C §§17000-17703) and must be licensed by the Corporations Commissioner (Fin C §17200). Real estate brokers are exempt from these requirements while they are acting in the course of, or incidental to, real estate transactions in which they are an agent or a party. Fin C §17006(a)(4). This exemption is "not available for any arrangement entered into for the purpose of performing escrows for more than one business." Fin C §17006(b). A broker may act as an escrow agent without an escrow license in a transaction in which he or she is also acting as a broker (54 Ops Cal Atty Gen 13 (1971)), but must obtain a license to act as an escrow agent in a transaction in which the broker is not providing brokerage services (43 Ops Cal Atty Gen 284 (1964)).

When acting under Fin C §17006(a)(4), the broker may charge a separate fee for escrow services. 44 Ops Cal Atty Gen 105 (1964). The Real Estate Commissioner has promulgated regulations on a broker's handling of funds as an escrow agent (10 Cal Code Regs §2951) and a broker's actions in handling an escrow (10 Cal Code Regs §2950).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.23 2. Decision to Use Broker-Escrow Agent

§2.23 2. Decision to Use Broker-Escrow Agent

The decision on whether to use a broker-affiliated escrow company must be carefully weighed. Generally, the escrow departments of banks or large title companies have greater resources and can provide a wider range of ancillary services than are available at a small, broker-owned escrow company. Counsel should generally advise against permitting brokers to act as both broker and escrow agent in the same transaction, because the broker's fiduciary duties become difficult to distinguish from the other duties the broker owes to the principal (see §§2.124-2.175), and—more importantly—because the escrow holder owes a fiduciary duty to both parties, not just the broker's principal. See *Colonial Sav. & Loan Ass'n v Redwood Empire Title Co.* (1965) 236 CA2d 186, 46 CR 16. It is unclear whether a broker-affiliated escrow agent could function as a truly neutral escrow agent.

ETHICAL CONSIDERATION: Attorneys who have a bona fide relationship with a principal in a real estate or personal property transaction are also exempt from the licensing requirements of the Escrow Law (Fin C §17006(a)(2)), but they should be aware of the conflicting duties that would arise from acting as both escrow agent and attorney in the same transaction.

For a discussion regarding liability of an escrow holder, see chap 15.

© The Regents of the University of California

II. BROKERS' SERVICES; SELECTING A BROKER

§2.24 A. Type of Services

Brokers provide a variety of services to parties in purchase and sale transactions. The mix of service and advice required by each client varies with the nature of the transaction and the sophistication of the client. At one extreme is the typical single-family home transaction. This client—buyer or seller—has no particular expertise in real estate transactions, and may be looking to the broker for a great deal of hand-holding through each step of the process. At the opposite end of the spectrum is the experienced commercial real estate investor who may have far more expertise in the real estate business than the broker. That client often does not need the broker for advice on the basics of buying and selling real estate, but relies on the broker either for assistance in marketing property and locating prospective buyers (if a seller) or for identifying potential acquisitions (if a buyer). In both instances, the broker is likely to be used as a go-between with the other party, from the negotiation stage through due diligence and close of escrow. Thus, especially in commercial transactions, the level of service and advice provided by the broker varies with the circumstances of the transaction, the relative sophistication of the parties, and the standard of care in the industry for similar transactions. See *Field v Century 21 Klowden-Forness Realty* (1998) 63 CA4th 18, 25-26, 73 CR2d 784; Restatement (Second) of Agency §379 (1958). On the broker's duties to the client, see §§2.124-2.152.

By knowing the local market, the broker is in a good position to provide accurate information on current property values and advice on how to market a seller's property or where to find property to meet a buyer's needs. Brokers also perform many routine functions, such as obtaining preliminary reports and distributing documents for review and execution. They can also provide advice and assistance to the parties in negotiating the terms of the transaction. Depending on the transaction, the broker may also offer other services, such as:

- Arranging for inspections;
- Assisting in evaluating the status of title;
- Suggesting various financing methods and sources;
- For investment properties, compiling financial information from the seller to facilitate the buyer's evaluation of the income potential of the property; and
- Obtaining comparable information from other sales that have occurred to assist the principal in evaluating value.

The range of services and other terms of the broker's relationship with the client—especially the broker's compensation—are subject to negotiation.

© The Regents of the University of California

§2.25 B. Factors to Consider in Selecting a Broker

The services brokers offer, and their expertise, experience, and knowledge of the market vary greatly. A prospective buyer or seller should look for a broker who is able to fulfill his or her specific needs. In selecting a broker, the buyer or seller should consider the following factors:

- *Broker's familiarity with the area in which the property is located.* A local broker is more likely to be well informed about prospective buyers or sellers in the area, the advantages and disadvantages of the area and of a particular parcel, local property values, sources of financing, and particular specialized local real estate forms or requirements. For instance, see the Residential Record Report ("3R Report") required in the sale or exchange of most residential buildings in the City and County of San Francisco, which contains, among other things, the construction date, permit history, and occupancy classification.
- *Broker's experience in handling the type of property under consideration and the type of transaction contemplated.* A broker who specializes in particular kinds of properties is more likely to know of prospective buyers or sellers and of available financing for that type of property. If the transaction will be complex or unusual, it is important that the broker have sufficient expertise to be able to understand and meet the client's needs.

Sellers often want to retain as much flexibility as possible through short-term and nonexclusive listings, but this consideration must be weighed against the likelihood that a broker with an exclusive or long-term listing will put more effort and resources into the transaction. See §§2.56-2.61 on types of listing agreements; see §§2.44-2.53 on the requirements for a writing.

The broker's commission, although subject to negotiation, will be an additional expense of the sale. Even though the seller usually pays the commission, the amount affects the buyer in that it is a factor in the seller's calculation of an acceptable price. On compensation, see §§2.91-2.123.

© The Regents of the University of California

III. BROKER AS AGENT

§2.26 A. Agency Versus Contract Law

The broker-client relationship is governed by both agency and contract law. Although the broker's right to compensation depends on the existence of a written agreement (CC §1624(a)(4); see §§2.44-2.53), an agency relationship may be created without either consideration (CC §2308; *Leno v YMCA* (1971) 17 CA3d 651, 95 CR 96) or a writing (*Steiner v Rowley* (1950) 35 C2d 713, 221 P2d 9). Thus, a broker without an enforceable contractual claim for a commission may still be subject to the fiduciary duties of the principal-agent relationship, the breach of which may render the broker liable for damages (*Steiner v Rowley, supra*) or subject to disciplinary action by the Real Estate Commissioner (*Buckley v Savage* (1960) 184 CA2d 18, 7 CR 328).

On brokers as agents, see California Real Estate Brokers: Law and Litigation, chap 3 (Cal CEB 2009).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.27 B. Creation of Agency Without Written Contract

§2.27 B. Creation of Agency Without Written Contract

An agency relationship is usually created between a seller and broker through a written listing or commission agreement; however, a written agreement is not required to establish an agency relationship. (Note, however, that a broker without a writing that satisfies the Statute of Frauds (CC §1624(a)(4)) will be unable to recover his or her commission. See §§2.43, 2.48.) Conversely, although a buyer-broker relationship can be created by a written agreement, they are not generally used in practice. Absent a written agreement, an agency relationship can be created by the following:

- Agreement of the parties, whether express or implied (see §2.28);
- Ratification of previously unauthorized acts of the agent (see §2.29); or
- Estoppel (or ostensible agency) (see §2.30).

California has substantially codified these common law agency principles. CC §§2295-2400.

© The Regents of the University of California

§2.28 1. Agency by Express or Implied Agreement

An agency is generally created by an express agreement, which may or may not be in writing. CC §§2299, 2307. No special formalities are required to create an agency, however, and the existence of an agency relationship may be inferred from the parties' actions. *Zander v Texaco, Inc.* (1968) 259 CA2d 793, 66 CR 561. Although no formalities are required, the parties must intend that the relationship exist, and this intent must be disclosed by either their express agreement or their actions. *Nizuk v Gorges* (1960) 180 CA2d 699, 4 CR 565.

The existence of agency is a question of fact for the trial court. California courts have been inclined to find the existence of an agency relationship when it is necessary to impose a fiduciary obligation on the broker to protect the seller against injury. *Skopp v Weaver* (1976) 16 C3d 432, 440, 128 CR 19 ("No California decision has held a realtor exempt from fiduciary obligation to the seller when the realtor has in fact acted to the seller's detriment").

© The Regents of the University of California

§2.29 2. Agency by Ratification

An agency may also be created when the principal ratifies previously unauthorized actions. CC §2307. Ratification occurs when the purported agent has held itself out as representing the principal (*Anderson v Fay Improvement Co.* (1955) 134 CA2d 738, 748, 286 P2d 513) and the principal then accepts the benefits of the purported agent's actions (CC §2310; *Rakestraw v Rodriques* (1972) 8 C3d 67, 104 CR 57). The third party is bound only when ratification occurs and may withdraw at any prior time. 3 Witkin, Summary of California Law, *Agency and Employment* §139 (10th ed 2005).

© The Regents of the University of California

§2.30 3. Ostensible Agency

Ostensible agency, also called agency by estoppel, arises when the principal either intentionally or negligently causes a third party to believe that another person is the principal's agent. CC §2300. Unlike agency by ratification (see §2.29), ostensible agency rests on statements, acts, or neglect by the principal that lead a third party to believe that an agency relationship exists. *Hill v Citizens Nat'l Trust & Sav. Bank* (1937) 9 C2d 172, 69 P2d 853. The California courts have always treated ostensible agency as resting on estoppel principles. *Lee v Helmco, Inc.* (1962) 199 CA2d 820, 19 CR 413; *Keppelman v Heikes* (1952) 111 CA2d 475, 245 P2d 54 (principal not allowed to use lack of agency as defense against third party who relied in good faith on principal's acts). If a principal's acts lead others to believe, in good faith, that he conferred authority on an agent, the principal cannot assert against those third persons that he did not intend to confer such power. *Preis v American Indem. Co.* (1990) 220 CA3d 752, 761, 269 CR 617.

A principal will thus be liable for an agent's acts under ostensible authority if (*Mejia v Community Hosp.* (2002) 99 CA4th 1448, 1456, 122 CR2d 233; see also CC §2300):

- The third party dealing with the agent believes in the agent's authority and such belief is reasonable;
- The belief is generated by some act or neglect of the principal sought to be charged; and
- The third person, in relying on the agent's apparent authority, is not guilty of negligence.

The ostensible authority of an agent generally is established through the acts or declarations of the principal—*not* the agent. *Jacoves v United Merchandising Corp.* (1992) 9 CA4th 88, 103, 11 CR2d 468. Additionally, a principal's failure to promptly disaffirm an agent's conduct on his or her behalf constitutes a ratification. *Norcal Mut. Ins. Co. v Newton* (2000) 84 CA4th 64, 79, 100 CR2d 683.

Ostensible agency has been invoked to permit a buyer to recover the downpayment from a brokerage firm for the actions of a nonmember broker who occupied space in the firm's offices and shared commissions. *Peterson v Ryan* (1951) 108 CA2d 41, 238 P2d 117.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/ C. Residential Disclosure Requirements on Agency Relationship/§2.31 1. Disclosure of Agency and Confirmation Forms

C. Residential Disclosure Requirements on Agency Relationship

§2.31 1. Disclosure of Agency and Confirmation Forms

Real estate agents in sales transactions (including leases for more than 1 year) involving residential property containing one to four dwelling units or mobilehomes must provide written disclosures to both the buyer and the seller on the available agency relationships. CC §§2079.13-2079.24. Moreover, the principals must confirm in writing the particular agency relationship selected (see §2.37).

Delivery of the completed disclosure form required by CC §2079.16 (see §2.36) must be made by:

- The listing agent to the seller before (or when) entering into the listing agreement (CC §2079.14(a));
- The selling agent to the seller as soon as practicable before (or when) presenting an offer (thus, sellers generally receive a copy of this form twice, even when listing agent and selling agent are with the same brokerage) (CC §2079.14(b)); and
- The selling agent to the buyer as soon as practicable before (or at the time of) execution of the buyer's offer (CC §2079.14(d)).

NOTE: The form often cannot be delivered before the listing agreement, presentation of the offer, or execution of the buyer's offer; so, instead, it is delivered at the same time as (but not after) these other documents.

The "selling agent" is the agent who procures the buyer. CC §2079.13(n). The selling agent may be the buyer's agent only, a dual agent or, in rare circumstances, the agent of the seller only (see §2.32). A selling agent who does not also represent the seller may be known as the "cooperating agent" or sometimes simply as the "buyer's agent." Usually, the disclosure form must be signed by the seller or buyer, acknowledging receipt. CC §2079.14.

The disclosure form merely describes the possible types of agency relationships that may be chosen. It does not disclose the particular type of agency relationship that, in fact, will exist. Disclosure of the actual type of agency relationship (*i.e.,* confirmation of that agency relationship) is made in a separate form prescribed by CC §2079.17. See §2.37. This confirmation form must be given to the buyer and the seller as soon as practicable, although the statute suggests that the confirmation is normally not made until an offer is presented to the seller (and often is contained in the offer itself). CC §2079.17(a)-(b). Thus, the disclosure form describing the various types of agency relationships may be given to buyers and sellers before all the forms confirming the actual relationship; but they are usually delivered simultaneously.

An agent who arranges financing in connection with a sale, lease, or exchange of real property must disclose this fact in writing to all parties to the transaction within "24 hours" (presumably after the agent first undertakes this role). Bus & P C §10177.6.

The agency disclosure statutes make no distinction between brokers and salespersons (who are now referred to as the agent and the associate licensee, respectively, because the agency relationship is deemed to exist between the client and broker, since the salesperson cannot contract on his or her own). See §§2.13-2.21 on the relationship between the broker and salesperson.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.32 2. Failure to Comply With Agency Disclosure Requirements

§2.32 2. Failure to Comply With Agency Disclosure Requirements

Civil Code §§2079.13-2079.24 provide no penalties for failure to confirm the agency relationship. In *Huijers v DeMarrais* (1992) 11 CA4th 676, 14 CR2d 232, a dual agent (who represented the buyer before approaching the sellers) failed to give the required disclosure when the listing was obtained, which made the listing agreement voidable at the sellers' option, thus relieving them from their obligation to pay the commission. The broker did make proper agency disclosures when the purchase contract was executed, and the sellers were not relieved of their obligations under that agreement.

© The Regents of the University of California

§2.33 3. Agency Elections

There are a variety of agency election options in the typical sales transaction. Most commonly, one agent represents only the seller and another represents only the buyer, but other permutations exist. A common misconception, even among experienced brokers, is that every party in a transaction is represented by an agent; but the parties' agreement, which may be established in writing by the buyer's and seller's acceptance of the brokers' agency elections, can establish different arrangements. The listing agent may elect to be the seller's agent only or a dual agent. The agent who procures the buyer ("selling agent") may elect to be a dual agent or the seller's agent only or (unless also acting as the listing agent) may elect to be the buyer's agent only. If an agent is both the listing and the selling agent and elects to be the seller's agent only, then the agent furnishes services to the buyer on behalf of the seller, and the buyer is unrepresented in the transaction. An agent who both lists and sells, however, is prohibited from representing the buyer only. CC §2079.18. As a consequence, no salesperson in the office of the listing broker can purport to represent the buyer exclusively. An agency relationship exists between the seller and the broker (not the salesperson) from the time the listing is signed, and that relationship cannot later be abrogated.

© The Regents of the University of California

§2.34 4. Change in Agency Election

Agency elections can be changed as long as the change is made before the agency services are performed. For example, an agent may elect to act as the buyer's exclusive agent when making an offer on property listed with another agent. If the offer is rejected and the buyer chooses to make an offer on one of the agent's own listings, the agency election must be changed to dual agency, because an agent cannot be the buyer's agent exclusively when the broker is also the listing agent. CC §2079.18.

© The Regents of the University of California

§2.35 5. Dual Agency of Listing Agents

Dual agency, in which the same broker represents both buyer and seller, is fairly common because listing agents frequently sell their own listings. Dual agency also arises when two different sales agents working under the same broker represent the parties, whether or not the two agents are in the same office of their common broker (because the agency relationship is deemed to exist at the broker level). CC §2079.13(d).

Authorization to act as a dual agent generally should be obtained from the seller when the listing agreement is executed. Typically, the agent will not know in advance whether it will procure the buyer (or whether another agent in the firm may do so). Sellers may agree to dual agency because they are retaining the broker for the express purpose of finding a suitable buyer; therefore, they do not want to limit the broker's ability to do so by preventing the broker from presenting the property to its own buyer-clients. See §2.129 for the benefits and disadvantages of dual agency.

If the seller refuses to permit the listing agent to act as a dual agent and represent the buyer as well, the listing agent may refer the buyer to an agent with another brokerage or the buyer could remain unrepresented. For a further discussion of dual agency and conflicts of interest, see §§2.129-2.130.

For an extensive discussion, and strong criticism, of former CC §§2373-2382 (now CC §§2079.13-2079.24), see Bernhardt, *Broker's Agency Disclosure Law: Misinformation or Disinformation?*, 11 CEB Real Prop L Rep 113 (July 1988).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.36 6. Form: Disclosure of Agency Relationship (CC §2079.16)

§2.36 6. Form: Disclosure of Agency Relationship (CC §2079.16)

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

2.36-1 Disclosure of agency relationship

DISCLOSURE REGARDING
REAL ESTATE AGENCY RELATIONSHIP
(As required by the Civil Code)

When you enter into a discussion with a real estate agent regarding a real estate transaction, you should from the outset understand what type of agency relationship or representation you wish to have with the agent in the transaction.

SELLER'S AGENT

A Seller's agent under a listing agreement with the Seller acts as the agent for the Seller only. A Seller's agent or a subagent of that agent has the following affirmative obligations:

To the Seller:

A fiduciary duty of utmost care, integrity, honesty, and loyalty in dealings with the Seller.

To the Buyer and the Seller:

(a) Diligent exercise of reasonable skill and care in performance of the agent's duties.

(b) A duty of honest and fair dealing and good faith.

(c) A duty to disclose all facts known to the agent materially affecting the value or desirability of the property that are not known to, or within the diligent attention and observation of, the parties.

An agent is not obligated to reveal to either party any confidential information obtained from the other party which does not involve the affirmative duties set forth above.

BUYER'S AGENT

A selling agent can, with a Buyer's consent, agree to act as agent for the Buyer only. In these situations, the agent is not the Seller's agent, even if by agreement the agent may receive compensation for services rendered, either in full or in part from the Seller. An agent acting only for a Buyer has the following affirmative obligations:

To the Buyer:

A fiduciary duty of utmost care, integrity, honesty, and loyalty in dealings with the Buyer.

To the Buyer and Seller:

(a) Diligent exercise of reasonable skill and care in performance of the agent's duties.

(b) A duty of honest and fair dealing and good faith.

(c) A duty to disclose all facts known to the agent materially affecting the value or desirability of the

property that are not known to, or within the diligent attention and observation of, the parties.

An agent is not obligated to reveal to either party any confidential information obtained from the other party that does not involve the affirmative duties set forth above.

AGENT REPRESENTING BOTH SELLER AND BUYER

A real estate agent, either acting directly or through one or more associate licensees, can legally be the agent of both the Seller and the Buyer in a transaction, but only with the knowledge and consent of both the Seller and the Buyer.

In a dual agency situation, the agent has the following affirmative obligations to both the Seller and the Buyer:

(a) A fiduciary duty of utmost care, integrity, honesty, and loyalty in the dealings with either the Seller or the Buyer.

(b) Other duties to the Seller and the Buyer as stated above in their respective sections.

In representing both Seller and Buyer, the agent may not, without the express permission of the respective party, disclose to the other party that the Seller will accept a price less than the listing price or that the Buyer will pay a price greater than the price offered.

The above duties of the agent in a real estate transaction do not relieve a Seller or Buyer from the responsibility to protect his or her own interests. You should carefully read all agreements to ensure that they adequately express your understanding of the transaction. A real estate agent is a person qualified to advise about real estate. If legal or tax advice is desired, consult a competent professional.

Throughout your real property transaction you may receive more than one disclosure form, depending on the number of agents assisting in the transaction. The law requires each agent with whom you have more than a casual relationship to present you with this disclosure form. You should read its contents each time it is presented to you, considering the relationship between you and the real estate agent in your specific transaction.

This disclosure form includes the provisions of Sections 2079.13 to 2079.24, inclusive, of the Civil Code set forth on the reverse hereof. Read it carefully.

_ _[*Agent*]_ _ __[*Signature of buyer/seller*]__
_ _[*Date*]_ _ _ _[*Date*]_ _

__[*Signature of associate licensee*]__ __[*Signature of buyer/seller*]__
_ _[*Date*]_ _ _ _[*Date*]_ _

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.37 7. Form: Confirmation of Agency Relationship (CC §2079.17)

§2.37 7. Form: Confirmation of Agency Relationship (CC §2079.17)

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

2.37-1 Confirmation of agency relationship

_ _[*Name of listing agent*]_ _ **is the agent of (check one):**

[ ] the seller exclusively; or

[ ] both the buyer and seller.

_ _[*Name of selling agent if not the same as the listing agent*]_ _ **is the agent of (check one):**

[ ] the buyer exclusively; or

[ ] the seller exclusively; or

[ ] both the buyer and seller.

Comment: Civil Code §2079.17 requires this form to be used in residential transactions, in addition to the disclosures required by CC §2079.14 (see §§2.31-2.35). Although general agency principles require the disclosure of dual agency in both commercial and residential transactions, it has not been held that disclosure must be in writing in a commercial transaction, although it certainly is better practice to do so. In residential transactions, the required written disclosure form must be included either in the purchase and sale agreement or in a separate writing executed or acknowledged before or coincident with the execution of that agreement. If the listing agent's confirmation is a separate writing, it must be executed or acknowledged by the seller and the listing agent. CC §2079.17(b). If the selling agent's confirmation is a separate writing, it must be signed by the seller, the buyer, and the selling agent. CC §2079.17(a).

© The Regents of the University of California

§2.38 D. Unintended Dual Agency

Although the seller usually pays the broker's commission, that fact alone does not prevent the broker from being the agent of the buyer, either exclusively or as a dual agent (*Wolf v Price* (1966) 244 CA2d 165, 52 CR 889), and this dual role can be the source of disputes and potential breaches of fiduciary duty (see §2.129). Normally, the broker is the agent of the party who first employs the broker. *Stephens v Ahrens* (1919) 179 C 743, 178 P 863. Frequently, however, a real estate transaction involves two principals and only one broker, who was originally retained by the seller but who also works with the buyer to complete the sale. In this situation, there is a common misunderstanding that the broker must represent both parties, but that is incorrect. Agency election remains subject to the agreement of the parties and the broker; in the absence of an express agreement, however, it will be determined by the parties' conduct. When one party has retained the broker, an agency relationship between the broker and the other party may arise from the broker's acceptance of duties and responsibilities to that party. See, *e.g., Whiteman v Leonard Realty Co.* (1961) 189 CA2d 373, 11 CR 211 (buyer's broker held to be seller's agent in undertaking to transmit escrow instructions); *Wright v Lowe* (1956) 140 CA2d 891, 296 P2d 34 (broker's agreement to convey buyer's counteroffer to seller made broker buyer's agent for that purpose).

The payment of, or obligation to pay, compensation to an agent by the seller or the buyer does not necessarily determine a particular agency relationship. CC §2079.19. In the absence of other factors, however, payment of a commission is strong evidence of an agency relationship between the broker and the party paying the fee. *Standard Realty & Dev. Co. v Ferrera* (1957) 151 CA2d 514, 311 P2d 855.

PRACTICE TIP: Because an agency relationship can arise without any express agreement between the parties, a broker should protect itself and the parties by making sure that agency relationships are disclosed to and confirmed by all parties in writing (as required in residential transactions).

© The Regents of the University of California

§2.38A E. Broker Acting in Non-Agency Capacity

"An agent is one who represents another… in dealings with third persons." CC §2295. There are times when a broker is not acting as an agent and is performing services that do not require a license. Examples include:

- In the preliminary stages of negotiating a listing or representation agreement—before the client retains the broker;
- In routine discussions with other industry members concerning market trends, recent transactions, etc.; and
- In providing consulting services that do not require the performing party to be a real estate licensee.

Although brokers still have obligations to parties with whom they do not have an agency relationship, no fiduciary duty arises in its absence. In *Stetler v Greenpoint Mortgage Funding Inc.* (ED Cal, Jan. 23, 2008) 2008 US Dist Lexis 4880, a borrower sued a mortgage broker whom, it alleged, had received undisclosed kickback payments from the lender. The court granted the mortgage broker summary judgment, holding that the broker did not owe a fiduciary duty to the borrower when their agreement provided that the broker was an independent contractor and not the borrower's agent and disclosed that the lender may compensate the broker. If the broker had been the borrower's agent, the details of any payments from the lender would have had to have been disclosed. See §2.135. The statutory scheme in some other states (*e.g.,* Colorado) permits a broker to declare itself a "transaction broker," which is not an agent of either the buyer or the seller. Colo Rev Stat §12-61-802. *Stetler* suggests that the same result could be obtained in California with appropriate contract language.

© The Regents of the University of California

§2.39 F. Multiple Listing Service

The multiple listing service (MLS) is usually sponsored by a local Board of Realtors® and provides a means for brokers to refer listings to other real estate licensees through a central information exchange. In California, the MLS is governed by CC §§1086-1090 and is defined as a facility for cooperation between agents, through which agents establish legal relationships with respect to listed properties. CC §1087. The service compiles and publishes listings submitted by participating brokers. A broker may not submit a listing to an MLS without the owner's authorization. CC §1088. Appraisers may use the MLS to establish legal relationships with respect to listed properties or to prepare market evaluations and appraisals of real property. CC §1087.

© The Regents of the University of California

§2.40 1. Subagency

Traditionally, the MLS required all listings submitted to contain an automatic unilateral offer of subagency to all MLS participants. In California, the MLS abandoned the automatic subagency requirement and created a system in which subagency is the exception rather than the rule. The MLS provides for a unilateral offer to share compensation rather than a unilateral offer of subagency. This system avoids many of the conflicts and liabilities inherent in subagency, particularly the dual agency problem, because the selling broker can now represent the buyer without becoming a dual agent as a result of a unilateral offer of subagency. On dual agency, see §§2.129-2.130. The National Association of Realtors® has also deleted the mandatory offer of subagency, making it optional. Many form listing agreements still give the broker the right to appoint subagents (see California Association of Realtors® form in §2.57) if the broker chooses to do so, but the MLS no longer requires it.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.41 2. Nonmember Access to Multiple Listing Services

§2.41 2. Nonmember Access to Multiple Listing Services

Before 1976, the MLS limited access to its listings to members of its sponsoring Boards of Realtors®, but *Marin County Bd.of Realtors v Palsson* (1976) 16 C3d 920, 130 CR 1, held that such restrictions on access violate the Cartwright Act (Bus & P C §§16700-16770). See also *Glendale Bd. of Realtors v Hounsell* (1977) 72 CA3d 210, 139 CR 830. California courts have also rejected restrictions on MLS access based on:

- Illegal group boycott (*People v National Ass'n of Realtors* (1981) 120 CA3d 459, 174 CR 728; board's refusal to accept any but exclusive right-to-sell listings defeated broker's right to negotiate other types of listings); and
- Price fixing in violation of the Cartwright Act and the unlawful competition statutes (Bus & P C §§16600-17365) (*Feldman v Sacramento Bd. of Realtors* (1981) 119 CA3d 739, 174 CR 231; board policies that encouraged equal commission splits and discouraged brokers from negotiating different arrangements unreasonably restricted competition).

These holdings have broadened the category of potential MLS users to include all licensees who wish to subscribe to the MLS, rather than board members only. Access to the MLS may, however, be restricted to licensed brokers and salespersons. *Derish v San Mateo-Burlingame Bd. of Realtors* (1982) 136 CA3d 534, 186 CR 390.

The federal courts have also examined the anticompetitive effects of MLSs, but with differing results. Although the Cartwright Act provides a separate state law basis for the California decisions, and thus the California courts cannot be required to accept the federal antitrust interpretation, it is interesting to note the federal holdings. See *Freeman v San Diego Ass'n of Realtors* (9th Cir 2003) 322 F3d 1133 (11 broker associations, which combined MLS databases into single database operated by single entity that charged fixed, inflated fee to subscribers, engaged in price-fixing in violation of the prohibition of contracts in restraint of trade (15 USC §1(e)) under the Sherman Antitrust Act (15 USC §§1-7)); *Pope v Mississippi Real Estate Comm'n* (5th Cir 1989) 872 F2d 127 (upholding tie-in requirement between board membership and right to join MLS); *U.S. v Realty Multi-List, Inc.* (5th Cir 1980) 629 F2d 1351 (exclusion from MLS had anticompetitive effects and, unless counterbalanced by some direct benefit to competition, regulation must fail).

© The Regents of the University of California

§2.42 G. Extent of Broker's Authority to Bind Principal

A real estate broker's authority is limited to that actually or ostensibly conferred by the principal. CC §2315. See §§2.28-2.30. The listing agreement should specify the extent of the broker's authority because an agent is authorized by statute to do everything "necessary or proper and usual" to carry out the purpose of the agency. CC §2319. Such broad implied authority invites disputes about what is proper and usual.

Generally, the broker's authority is limited to negotiating the terms of the transaction; the broker has no authority to bind the seller contractually, even if the buyer makes an unconditional offer on all the terms and conditions in the listing agreement. *Holland v McCarthy* (1916) 173 C 597, 160 P 1069. For example, the broker may not deliver the seller's deed to the buyer (*Keele v Clouser* (1928) 92 CA 526, 268 P 682) or sign a contract of sale on the principal's behalf (*Lyne v Bonner* (1954) 129 CA2d 743, 277 P2d 941) without specific authority to do so. Only the principal, not a third party, can raise the issue of the broker's lack of authority. *Mitchell v Locurto* (1947) 79 CA2d 507, 179 P2d 848.

A broker is rarely given express authority to accept the purchase price, as distinguished from the deposit (see §2.68), on the seller's behalf. *Sarten v Pomatto* (1961) 192 CA2d 288, 13 CR 588 (seller authorized broker to accept deposit). Even when the broker is expressly authorized to negotiate the sale, courts have not found authority to collect the purchase price. *Ernst v Searle* (1933) 218 C 233, 22 P2d 715. If the seller has led the buyer to believe that the agent can receive the purchase price, however, then ostensible authority exists (see §2.30), and the seller will not be able to recover from the buyer if the broker misappropriates the funds. *Hicks v Wilson* (1925) 197 C 269, 240 P 289. A broker who does receive the purchase price for the seller must be careful to comply with the Real Estate Law and the regulations of the Real Estate Commissioner on brokers' handling of clients' funds. Bus & P C §10145; 10 Cal Code Regs §§2830.1-2836.

© The Regents of the University of California

IV. CONTRACTING WITH BROKER

A. Elements Applicable to Both Sellers and Buyers

§2.43 1. Essentials of Contract

Although an agency relationship and its attendant duties can be established without a written contract, a broker without a writing that satisfies the Statute of Frauds (CC §1624(a)(4)) will be unable to recover his or her commission. See §2.48. Furthermore, the broker will not be able to recover in quantum meruit the value of any brokerage or other incidental services provided to the client (see §§2.44-2.53). *Phillippe v Shapell Indus.* (1987) 43 C3d 1247, 241 CR 22. Written broker-principal contracts generally grant limited agency authority to the broker and obligate the principal to compensate the broker if specified conditions are fulfilled.

Like any contract, an agreement with a broker requires these elements (CC §1550):

- Parties capable of contracting (see CC §§1556-1559);
- The parties' consent (see CC §§1565-1590);
- A lawful object (see CC §§1595-1599); and
- Sufficient cause or consideration (see §§1605-1615).

Contracts with real estate licensees are subject to additional requirements. A copy of any agreement authorizing or employing a real estate licensee must be delivered to the person signing it when the signature is obtained. Bus & P C §10142; see §2.88. The broker's right to a commission depends on express authorization in the agreement. See §2.97. Other requirements are discussed in connection with the forms for listing agreement provisions that satisfy those requirements. See §§2.62-2.88.

On contracting with brokers, see California Real Estate Brokers: Law and Litigation, chap 2 (Cal CEB 2009).

© The Regents of the University of California

2. Statute of Frauds

§2.44 a. Contents of Required Writing

An "agreement authorizing or employing an agent, broker, or any other person to purchase or sell real estate," to lease real property for a period longer than 1 year, or to procure a purchaser, seller, lessee, or lessor of real property, must be in writing. CC §1624(a)(4). To satisfy the Statute of Frauds, the writing need not contain all elements of a binding contract. See §2.43. If the document includes the essential terms of the agreement but their meaning is unclear, "the memorandum is sufficient under the Statute of Frauds if extrinsic evidence clarifies the terms with reasonable certainty and the evidence as a whole demonstrates that the parties intended to be bound." *Sterling v Taylor* (2007) 40 C4th 757, 55 CR3d 116. The writing must, however, establish the broker's authority to act for the principal (see §2.45), identify the property (see §2.46), and be signed by the principal (see §2.47).

The words "or any other person" in CC §1624(a)(4) mean that even a finder or an intermediary (see §2.5) must have a written agreement in order to recover a fee in a real property transaction. Under the Statute of Frauds, a finder cannot assert a breach of contract claim based on an oral agreement. Unlike a broker, however, a finder is free to pursue an ordinary misrepresentation claim or sue on a theory of estoppel. See §§2.50-2.51. Compare CC §1624(a)(4) with *Zalk v General Exploration Co.* (1980) 105 CA3d 786, 164 CR 647, in which a finder was able to enforce an oral agreement because the agreement was for locating a company to be acquired rather than locating real property. For further discussion of the Statute of Frauds, see §4.13.

© The Regents of the University of California

§2.45 (1) Employment of Broker

The writing must establish the fact of employment for the broker to act or to negotiate a sale for the owner. CC §1624(a)(4). Some courts have interpreted this requirement rather strictly, so any memorandum on which a broker intends to rely should use words that have typically denoted an employment relationship, such as "appoint," "employ," or "authorize." (Other language that has been held sufficient to show an employment relationship includes: "you may have the listing with one or two other realtors" (*Rogers v Grua* (1963) 215 CA2d 1, 30 CR 39), "go ahead" (*Spitler v Avery* (1961) 189 CA2d 811, 11 CR 724), and "take it up" (*Bruner v Van's Mkts.* (1951) 103 CA2d 135, 229 P2d 56).

Some older cases dealing with this issue have held that writings that set forth the terms on which the principal is willing to sell or buy, without specific language appointing the broker, do not comply with CC §1624(a)(4). See, *e.g. Franklin v Hansen* (1963) 59 C2d 570, 30 CR 530. In *Seck v Foulks* (1972) 25 CA3d 556, 102 CR 170, however, the Statute of Frauds was satisfied when the broker jotted down the terms of the sale, including the commission, on the back of his business card and had the seller date and sign it, despite the fact that no specific language of appointment was used. In the authors' opinion, language that demonstrates an agreement to pay a commission or fee for specified services or objectives accomplished should be sufficient to satisfy the requirement, especially if the client has accepted the benefit of the broker's performance.

© The Regents of the University of California

§2.46 (2) Identity of Property

The property that is the subject of the agency relationship must be described with sufficient clarity to permit reasonable identification. See, *e.g., Wolf v Price* (1966) 244 CA2d 165, 52 CR 889. An exact legal description is not required, and parol evidence may be admitted to explain the meaning of the written description. A description such as "my house," when the principal owned only one house in the state, has been held sufficient. *Pray v Anthony* (1929) 96 CA 772, 274 P 1024. Courts have not, however, admitted extrinsic evidence to identify the property when a writing contained no description at all. *Proulx v Sacramento Valley Land Co.* (1912) 19 CA 529, 126 P 509.

© The Regents of the University of California

§2.47 (3) Execution of the Writing

The writing need not be signed by both parties, but it must be subscribed by or on behalf of "the party to be charged." CC §1624(a). The signature of an authorized agent of a corporation is sufficient to bind the corporation. *Marks v Walter G. McCarty Corp.* (1949) 33 C2d 814, 205 P2d 1025.

The Statute of Frauds is intended to establish the existence of a contract (but not necessarily all its terms); therefore, the writing can be signed after the services are rendered or even after the sale has closed and title has been transferred. *Estate of Rule* (1944) 25 C2d 1, 152 P2d 1003, disapproved on other grounds in *Parsons v Bristol Dev. Co.* (1965) 62 C2d 861, 44 CR 767. A promissory note for the broker's commission, signed by the seller after closing, satisfied the Statute of Frauds in *Fellom v Adams* (1969) 274 CA2d 855, 79 CR 633.

In commercial or industrial transactions, there may be no memorandum on which the broker can rely until the parties execute the contract of sale or the escrow instructions. Both escrow instructions (*Beazell v Schrader* (1963) 59 C2d 577, 30 CR 534) and a deposit receipt (*Mitchell v Johnston* (1956) 140 CA2d Supp 982, 298 P2d 170) have been held sufficient as writings, but the broker's rights are then contingent on completion of the sale. If a sale is not completed because of mutual rescission or the buyer's breach (*Paulsen v Leadbetter* (1968) 267 CA2d 148, 72 CR 819), CC §1624(a) requires a showing that the seller and the broker intended the commission to be earned on execution of the agreement. In *Rader Co. v Stone* (1986) 178 CA3d 10, 223 CR 806, a broker in a lease transaction was able to satisfy the subscription requirement because a landlord's agent had signed a Realtor Registration Form completed by the broker, which, together with a series of other papers, was held to constitute a written contract to pay a commission.

NOTE: The Uniform Electronic Transactions Act (CC §§1633.1-1633.17) provides that an electronic record ("a record created, generated, sent, communicated, received, or stored by electronic means") or electronic signature will satisfy the legal requirements of a writing or signature. CC §1633.8. The term "electronic signature" should be distinguished from the term "digital signature." A digital signature is a digital code that can be attached to an electronically transmitted message to uniquely identify the sender so that if even one bit in the message changes on its way, the signature will not verify at the other end. The use of digital signatures is permitted in transactions with public entities. Govt C §16.5; 2 Cal Code Regs §§22000-22005.

See also the federal Electronic Signatures in Global and National Commerce Act (15 USC §§7001-7031) (Pub L 106-229, 114 Stat 464), which also validates electronic signatures and records. State law, however, may supersede the federal law if certain conditions are met. 15 USC §7002.

© The Regents of the University of California

§2.48 b. No Compensation Without a Writing

The California Supreme Court has extensively analyzed the writing requirement and concluded that, except in very limited situations (*i.e.,* when the broker has performed services that are not broker related or incidental to broker-related services), a broker cannot recover compensation from his or her principal unless the broker has a writing that satisfies the Statute of Frauds. *Phillippe v Shapell Indus.* (1987) 43 C3d 1247, 241 CR 22. Courts have applied the statute to broker-client relationships in virtually all categories of real property transactions, including options (*Pacific S.W. Dev. Corp. v Western Pac. R.R.* (1956) 47 C2d 62, 301 P2d 825), assignments of contracts to purchase real property (*King v Tilden Park Estates* (1958) 156 CA2d 824, 320 P2d 109), and exchanges (*Zimmerman v Bank of America* (1961) 191 CA2d 55, 12 CR 319).

Without a writing, the value of the broker's services cannot be recovered, even if the principal has taken advantage of the services and substantially benefited from them. *Augustine v Trucco* (1954) 124 CA2d 229, 268 P2d 780. Thus, a buyer's broker or cooperating brokers may have an enforceable right to share the commission only if there is an express written agreement, *e.g.,* the seller's broker's listing agreement. See *Enea v Coldwell Banker/Del Monte Realty* (Bankr ND Cal 1998) 225 BR 715. The broker may be able to recover a commission for the sale of personal property (*Marks v Walter G. McCarty Corp.* (1949) 33 C2d 814, 205 P2d 1025) or for various nonbrokerage services without a writing as long as they are separable from real estate brokerage services (*Carey v Cusack* (1966) 245 CA2d 57, 54 CR 244). In *Hughes v Morrison* (1984) 160 CA3d 103, 206 CR 321, brokers were permitted to recover a commission when the original sale agreement was replaced by a new agreement between the same parties for the same property. The court concluded that, because the original broker played a substantial part in the renegotiation, the original commission agreement should apply. When the client clearly has used and benefited from the broker's services, a writing may be found to satisfy the Statute of Frauds even if it is not in the form of a traditional listing or commission agreement. *Torelli v J.P. Enters*. (1997) 52 CA4th 1250, 61 CR2d 76 (see §2.52); *Rader Co. v Stone* (1986) 178 CA3d 10, 223 CR 806 (see §2.47).

The Statute of Frauds, however, does not require that the writing indicate the amount of the broker's commission or even the broker's entitlement to compensation. *Barcelon v Cortese* (1968) 263 CA2d 517, 69 CR 657. If a writing demonstrates that the principal authorized the agent to act on his or her behalf, other provisions of the agreement, including the commission, may be proved by parol evidence. *Bruner v Van's Mkts.* (1951) 103 CA2d 135, 229 P2d 56. If no evidence exists in writing or from parol evidence on the amount of the commission, the courts will infer an agreement to pay reasonable compensation. *Beazell v Schrader* (1963) 59 C2d 577, 30 CR 534.

© The Regents of the University of California

c. Theories of Recovery in Absence of a Writing

§2.49 (1) Quasi-Contract Theory

A broker cannot recover from the seller on a quasi-contract theory, regardless of the amount of time, expense, or effort spent or substantial benefit conferred on the seller. *Beazell v Schrader* (1963) 59 C2d 577, 30 CR 534. This theory of recovery has been so roundly rejected by the courts that many recent attempts by brokers to recover commissions do not even raise it.

Brokers have, however, been allowed to recover under oral agreements on a quasi-contractual basis for nonbrokerage expenditures such as survey costs, costs of locating suitable sites, subdivision costs, and other indirect selling expenses. *Carey v Cusack* (1966) 245 CA2d 57, 54 CR 244. These nonbrokerage services must be clearly separable from brokerage services. *Carey v Cusack, supra*.

© The Regents of the University of California

§2.50 (2) Fraud and Misrepresentation

To recover for fraud, a plaintiff must show reasonable reliance on a defendant's misrepresentation. A licensed broker cannot, as a matter of law, establish this required element of reasonable reliance to recover on the client's oral promise to pay a commission because the broker is presumed to know that an oral commission agreement is unenforceable. *Phillippe v Shapell Indus.* (1987) 43 C3d 1247, 241 CR 22. The court, however, suggested that there may be other promises on which a licensed broker could reasonably rely and thus assert a claim for fraud. As an example, the court cited the broker's reliance on a representation that a written agreement had been executed in *Owens v Foundation for Ocean Research* (1980) 107 CA3d 179, 165 CR 571, overruled on other grounds in *Applied Equip. v Litton Saudi Arabia Ltd.* (1994) 7 C4th 503, 28 CR2d 475.

In contrast to a broker, a finder may seek recovery based on the principal's alleged misrepresentation, and the fact that an unwritten promise is unenforceable as a contract does not preclude an action for fraud. A finder, however, may seek recovery based on the principal's alleged misrepresentation and the unenforceability of an unwritten promise as a contract does not preclude an action for fraud. *Tenzer v Superscope, Inc.* (1985) 39 C3d 18, 216 CR 130. Mere proof that a promise was made but not fulfilled, however, is insufficient to prove fraud. Something more than nonperformance is required to prove an intent not to perform on the promise. (The court reserved for another day the question of whether licensed brokers may invoke equitable remedies to avoid the results of the Statute of Frauds.)

© The Regents of the University of California

§2.51 (3) Estoppel Theory

The theory of estoppel usually does not help a broker trying to collect a commission in the absence of a written contract. Many seller-broker disputes seem to present a prima facie case for invoking the equitable estoppel doctrine to prevent a reneging principal from raising the defense of the Statute of Frauds. See 13 Witkin, Summary of California Law, *Equity* §191 (10th ed 2005); *Domarad v Fisher & Burke* (1969) 270 CA2d 543, 76 CR 529. Courts generally have been unwilling to apply this theory, however, because it would permit precisely what the Statute of Frauds was designed to prevent: the oral assertion of a promise with no easily available contravention other than denial. *Phillippe v Shapell Indus.* (1987) 43 C3d 1247, 241 CR 22 (requires showing of actual fraud); *Pacific S.W. Dev. Corp. v Western Pac. R.R.* (1956) 47 C2d 62, 301 P2d 825. But compare these cases with *Tenzer v Superscope, Inc.* (1985) 39 C3d 18, 216 CR 130, in which the supreme court held that a finder, who need not be a licensed real estate broker, was entitled to invoke the doctrine of estoppel to overcome the Statute of Frauds.

© The Regents of the University of California

§2.52 d. Exceptions

The courts have recognized a few exceptions to the CC §1624(a)(4) requirement that agreements authorizing or employing brokers to purchase or sell real estate or to procure a buyer must be in writing:

- An agreement between a finder and a broker, providing for a fee to the finder for introducing the broker to prospective sellers or buyers, need not be in writing because no buyer or seller is a party to the agreement. *Grant v Marinell* (1980) 112 CA3d 617, 169 CR 414.
- Commission-sharing agreements between brokers are not subject to the Statute of Frauds. *Iusi v Chase* (1959) 169 CA2d 83, 337 P2d 79. See §2.52.
- An agreement between two brokers who cooperate in selling real property need not be in writing. *Holland v Morgan & Peacock Prop. Co.* (1959) 168 CA2d 206, 335 P2d 769. The cooperating broker's share can be recovered from the listing broker if the listing broker has a written contract with the seller, or if the entire commission has already been paid to the listing broker. *Iusi v Chase, supra*.
- A broker who is acting as a member of a joint venture is a principal rather than an agent, and the broker's authority to bind the coventurers in a real property transaction need not be in writing. *Foote v Posey* (1958) 164 CA2d 210, 330 P2d 651.
- An implied covenant of good faith may permit the broker to recover a commission even when the listing agreement has expired. For instance, in *Torelli v J.P. Enters.* (1997) 52 CA4th 1250, 61 CR2d 76, the buyer's offer included a commission to be split between Torelli and the buyer's broker. The seller's counteroffer did not change the commission terms. The counteroffer expired unaccepted. Later, the buyer's broker drafted an offer deleting Torelli's commission and reduced the purchase price by the amount of the commission. The court held that a seller cannot agree to sell the property to the buyer on substantially the same terms as those in a counteroffer without paying the broker the contemplated commission; to do so violates the implied covenant of good faith. The broker's right to a commission—predicated on finding a buyer for the seller—is not necessarily defeated just because the buyer and seller do not sign the precise piece of paper embodying the commission agreement, as long as a sufficient writing exists. 52 CA4th at 1257.

© The Regents of the University of California

§2.53 e. Modification of Listing Agreement

Contracts that are required to be in writing generally cannot be modified orally. CC §1698(c). However, an oral modification is enforceable if it is executed (CC §1698(b)), with the result that an oral modification to a listing agreement is enforceable if both parties have carried out the terms of the modification. *Realty Corp. of Am. v Burton* (1958) 162 CA2d 44, 327 P2d 948. For example, if a broker agrees to accept a smaller commission, and the owner then agrees to accept a lower sale price, the broker is bound by the oral modification. *Fidler v Schiller* (1963) 212 CA2d 569, 28 CR 48; *Lawrence Block Co. v Scholer* (1958) 166 CA2d 608, 333 P2d 396. A broker's oral agreement to receive his commission from the proceeds of the buyer's installment payments was enforced when the broker accepted partial payment from the downpayment and first installment but demanded full payment when the buyer defaulted on a later installment. *Waldteufel v Sailor* (1944) 62 CA2d 577, 144 P2d 894. In commercial transactions, it is not unusual for commissions to be renegotiated, and the better practice is to commit all such agreements to writing.

© The Regents of the University of California

§2.54 B. Seller-Broker Listing Agreements

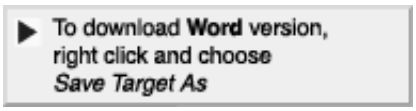
A listing agreement is simply an employment contract between the seller and the broker, and the parties are free to negotiate any terms that are lawful. *Blank v Borden* (1974) 11 C3d 963, 115 CR 31. The performance required of the broker, and the conditions under which the seller will become obligated to pay the broker's compensation, must be in the listing agreement. *Blank v Borden, supra*; *Seck v Foulks* (1972) 25 CA3d 556, 102 CR 170; see §2.97. Three commonly used types of listing agreements have evolved in the industry: exclusive right to sell (see §§2.56-2.57), exclusive agency (see §2.58), and open listing (see §2.59). See, *e.g., Tetrick v Sloan* (1959) 170 CA2d 540, 339 P2d 613; CC §1086(f). The three types of listings are distinguished by the conditions that must be fulfilled for the broker to earn the commission. No particular form of agreement is required to be used; the parties' rights are established by the provisions actually included in their agreement. It is the contents of the agreement, not its title, that the courts will consider controlling. See, *e.g., Coleman v Mora* (1968) 263 CA2d 137, 69 CR 166.

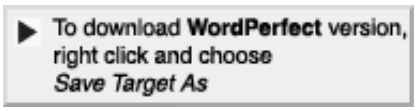
Any one of the common forms of listing agreement, or any hybrid agreement negotiated by the parties, may include a net listing arrangement (see §2.61) and may either allow or require the broker to cooperate (*i.e.,* share his or her commission with other brokers) and refer the listing to the local multiple listing service (see §2.75), or both.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.55 1. Listing Agreement Checklist

§2.55 1. Listing Agreement Checklist





When reviewing a listing agreement prepared by the broker, the attorney for the seller should pay particular attention to the following provisions:

- The amount of the commission, usually expressed as a percentage of the sales price. By law, all commissions are negotiable. Bus & P C §10147.5.
- The term of the listing agreement. A 3- or 6-month term is common. If the term is too short, the broker may not be sufficiently motivated to sell the property. If the term is too long, it may be difficult to switch to another broker if the first broker is not putting forth sufficient effort.
- Does the agreement specifically list what constitutes "due diligence" by the broker and the specific tasks the broker will perform? Industry forms rarely include such provisions.
- The language concerning when the commission is earned (as opposed to the time when payment is due). From the seller's standpoint, the commission should not be earned until the sale has closed, unless closing was prevented by the seller's breach of the sales agreement. Listing agreements frequently provide that the commission is earned when the broker produces a "ready, willing, and able buyer." Under such a provision, the seller may be liable for the commission once an unconditional contract is accepted, even if the buyer later refuses to complete the transaction (although the broker may have difficulty proving that a defaulting buyer was, in fact, "ready, willing, and able"). See §2.108. Some listing agreements may contain ambiguous language concerning when the commission is earned. For example, some may state that the commission is earned when the property is "sold."
- Is the broker expected to cooperate with other brokers, and, if so, how the commission is to be shared?
- Will the listing be submitted to the multiple listing service (residential transactions)? Sellers usually wish to get the broadest possible exposure of the property as quickly as possible.
- The price and terms of sale. Even though the sale terms in a listing agreement do not obligate the seller to sell to a buyer whose offer meets the terms, the broker may have earned a commission when he or she procures an offer that meets the specified terms.

© The Regents of the University of California

2. Types of Listing Agreements

a. Exclusive Right to Sell

§2.56 (1) General Characteristics

An exclusive right-to-sell listing gives the broker the right to the commission if the property is sold during the listing period by anyone, including the seller. *Lowe v Loyd* (1949) 93 CA2d 684, 209 P2d 851. The broker need not be the procuring cause (see §§2.99-2.105) and need not even have contacted the buyer. *Berzon v U.L.C. Corp.* (1969) 274 CA2d 690, 79 CR 277.

Listing agreements are strictly construed against the broker. Courts will not find an exclusive right-to-sell agreement unless it is expressly so designated. *E.A. Strout W. Realty v Gregoire* (1950) 101 CA2d 512, 225 P2d 585. An exclusive right-to-sell agreement must contain a definite termination date. If it does not, the broker will be subject to disciplinary action by the Real Estate Commissioner if the broker seeks compensation under the agreement. Bus & P C §10176(f). Provisions in many exclusive right-to-sell agreements entitle the broker to the full commission if the seller withdraws the property from the market (*Baumgartner v Meek* (1954) 126 CA2d 505, 272 P2d 552) or does something to the property that makes it unmarketable or substantially reduces its marketability (*Alderson v Houston* (1908) 154 C 1, 96 P 884). In *Blank v Borden* (1974) 11 C3d 963, 115 CR 31, the validity of such a commission-on-withdrawal clause was upheld. See §2.114.

Many exclusive right-to-sell listing agreements also contain a safety or protection clause that entitles the broker to the commission if the property is sold within a stated period after the listing expires to a buyer identified during the term of the listing. See §§2.115-2.116 on the safety clause. The CAR exclusive authorization and right-to-sell form is set forth in §2.57. It contains a commission-on-withdrawal clause and a limited safety clause.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.57 (2) Form: Residential Listing Agreement (Exclusive Authorization and Right to Sell) (CAR Form RLA)

§2.57 (2) Form: Residential Listing Agreement (Exclusive Authorization and Right to Sell) (CAR Form RLA)



CALIFORNIA ASSOCIATION OF REALTORS®

RESIDENTIAL LISTING AGREEMENT

(Exclusive Authorization and Right to Sell)

(C.A.R. Form RLA, Revised 2/09)

1. **EXCLUSIVE RIGHT TO SELL:** _____ ("Seller")
hereby employs and grants _____ ("Broker")
beginning (date) _____ and ending at 11:59 P.M. on (date) _____ ("Listing Period")
the exclusive and irrevocable right to sell or exchange the real property in the City of _____,
County of _____, Assessor's Parcel No. _____,
California, described as: _____ ("Property").

2. **ITEMS EXCLUDED AND INCLUDED:** Unless otherwise specified in a real estate purchase agreement, all fixtures and fittings that are attached to the Property are included, and personal property items are excluded, from the purchase price.
ADDITIONAL ITEMS EXCLUDED: _____
ADDITIONAL ITEMS INCLUDED: _____
Seller intends that the above items be excluded or included in offering the Property for sale, but understands that: **(i)** the purchase agreement supersedes any intention expressed above and will ultimately determine which items are excluded and included in the sale; and **(ii)** Broker is not responsible for and does not guarantee that the above exclusions and/or inclusions will be in the purchase agreement.

3. **LISTING PRICE AND TERMS:**
A. The listing price shall be: _____
_____ Dollars ($ _____)
B. Additional Terms: _____
_____

4. **COMPENSATION TO BROKER:**
Notice: The amount or rate of real estate commissions is not fixed by law. They are set by each Broker individually and may be negotiable between Seller and Broker (real estate commissions include all compensation and fees to Broker).
A. Seller agrees to pay to Broker as compensation for services irrespective of agency relationship(s), either ☐ _____ percent of the listing price (or if a purchase agreement is entered into, of the purchase price), or ☐ $ _____,
AND _____, as follows:
(1) If during the Listing Period, or any extension, Broker, Seller, cooperating broker, or any other person procures a buyer(s) who offers to purchase the Property on the above price and terms, or on any price and terms acceptable to Seller, (Broker is entitled to compensation whether any escrow resulting from such offer closes during or after the expiration of the Listing Period.)
OR (2) If within _____ calendar days **(a)** after the end of the Listing Period or any extension, or **(b)** after any cancellation of this Agreement, unless otherwise agreed, Seller enters into a contract to sell, convey, lease or otherwise transfer the Property to anyone ("Prospective Buyer") or that person's related entity: **(i)** who physically entered and was shown the Property during the Listing Period or any extension by Broker or a cooperating broker, or **(ii)** for whom Broker or any cooperating broker submitted to Seller a signed, written offer to acquire, lease, exchange or obtain an option on the Property. Seller, however, shall have no obligation to Broker under paragraph 4A(2) unless, not later than **3 calendar days** after the end of the Listing Period or any extension or cancellation, Broker has given Seller a written notice of the names of such Prospective Buyers.
OR (3) If, without Broker's prior written consent, the Property is withdrawn from sale, conveyed, leased, rented, otherwise transferred, or made unmarketable by a voluntary act of Seller during the Listing Period, or any extension.
B. If completion of the sale is prevented by a party to the transaction other than Seller, then compensation due under paragraph 4A shall be payable only if and when Seller collects damages by suit, arbitration, settlement or otherwise, and then in an amount equal to the lesser of one-half of the damages recovered or the above compensation, after first deducting title and escrow expenses and the expenses of collection, if any.
C. In addition, Seller agrees to pay Broker: _____
D. Seller has been advised of Broker's policy regarding cooperation with, and the amount of compensation offered to, other brokers.
(1) Broker is authorized to cooperate with and compensate brokers participating through the multiple listing service(s) ("MLS") by offering MLS brokers either ☐ _____ percent of the purchase price, or ☐ $ _____.
(2) Broker is authorized to cooperate with and compensate brokers operating outside the MLS as per Broker's policy.
E. Seller hereby irrevocably assigns to Broker the above compensation from Seller's funds and proceeds in escrow. Broker may submit this Agreement, as instructions to compensate Broker pursuant to paragraph 4A, to any escrow regarding the Property involving Seller and a buyer, Prospective Buyer or other transferee.
F. **(1)** Seller represents that Seller has not previously entered into a listing agreement with another broker regarding the Property, unless specified as follows: _____
(2) Seller warrants that Seller has no obligation to pay compensation to any other broker regarding the Property unless the Property is transferred to any of the following individuals or entities: _____
_____
(3) If the Property is sold to anyone listed above during the time Seller is obligated to compensate another broker: **(i)** Broker is not entitled to compensation under this Agreement; and **(ii)** Broker is not obligated to represent Seller in such transaction.

The copyright laws of the United States (Title 17 U.S. Code) forbid the unauthorized reproduction of this form, or any portion thereof, by photocopy machine or any other means, including facsimile or computerized formats. Copyright © 1991-2009, CALIFORNIA ASSOCIATION OF REALTORS®, INC. ALL RIGHTS RESERVED.

Seller acknowledges receipt of a copy of this page.
Seller's Initials (_____)(_____)

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

Print

Property Address: _____ Date: _____

5. **OWNERSHIP, TITLE AND AUTHORITY:** Seller warrants that: **(i)** Seller is the owner of the Property; **(ii)** no other persons or entities have title to the Property; and **(iii)** Seller has the authority to both execute this Agreement and sell the Property. Exceptions to ownership, title and authority are as follows: _____
6. **MULTIPLE LISTING SERVICE:** All terms of the transaction, including financing, if applicable, will be provided to the selected MLS for publication, dissemination and use by persons and entities on terms approved by the MLS. Seller authorizes Broker to comply with all applicable MLS rules. MLS rules allow MLS data about the Property to be made available by the MLS to additional Internet sites unless Seller gives Broker instructions to the contrary. MLS rules generally provide that residential real property and vacant lot listings be submitted to the MLS within 48 hours or some other period of time after all necessary signatures have been obtained on the listing agreement. However, Broker will not have to submit this listing to the MLS or can prohibit this listing or certain information from or about it from appearing on certain internet sites if, Broker submits to the MLS such an instruction signed by Seller (C.A.R. Form SEL or the locally required form). Information about this listing will be provided to the MLS of Broker's selection unless a form instructing Broker to the contrary is attached to this listing Agreement.
7. **SELLER REPRESENTATIONS:** Seller represents that, unless otherwise specified in writing, Seller is unaware of: **(i)** any Notice of Default recorded against the Property; **(ii)** any delinquent amounts due under any loan secured by, or other obligation affecting, the Property; **(iii)** any bankruptcy, insolvency or similar proceeding affecting the Property; **(iv)** any litigation, arbitration, administrative action, government investigation or other pending or threatened action that affects or may affect the Property or Seller's ability to transfer it; and **(v)** any current, pending or proposed special assessments affecting the Property. Seller shall promptly notify Broker in writing if Seller becomes aware of any of these items during the Listing Period or any extension thereof.
8. **BROKER'S AND SELLER'S DUTIES:** Broker agrees to exercise reasonable effort and due diligence to achieve the purposes of this Agreement. Unless Seller gives Broker written instructions to the contrary, Broker is authorized to order reports and disclosures as appropriate or necessary and advertise and market the Property by any method and in any medium selected by Broker, including MLS and the Internet, and, to the extent permitted by these media, control the dissemination of the information submitted to any medium. Seller agrees to consider offers presented by Broker, and to act in good faith to accomplish the sale of the Property by, among other things, making the Property available for showing at reasonable times and referring to Broker all inquiries of any party interested in the Property. Seller is responsible for determining at what price to list and sell the Property. **Seller further agrees to indemnify, defend and hold Broker harmless from all claims, disputes, litigation, judgments and attorney fees arising from any incorrect information supplied by Seller, or from any material facts that Seller knows but fails to disclose.**
9. **DEPOSIT:** Broker is authorized to accept and hold on Seller's behalf any deposits to be applied toward the purchase price.
10. **AGENCY RELATIONSHIPS:**
    A. **Disclosure:** If the Property includes residential property with one-to-four dwelling units, Seller shall receive a "Disclosure Regarding Agency Relationships" form prior to entering into this Agreement.
    B. **Seller Representation:** Broker shall represent Seller in any resulting transaction, except as specified in paragraph 4F.
    C. **Possible Dual Agency With Buyer:** Depending upon the circumstances, it may be necessary or appropriate for Broker to act as an agent for both Seller and buyer, exchange party, or one or more additional parties ("Buyer"). Broker shall, as soon as practicable, disclose to Seller any election to act as a dual agent representing both Seller and Buyer. If a Buyer is procured directly by Broker or an associate-licensee in Broker's firm, Seller hereby consents to Broker acting as a dual agent for Seller and such Buyer. In the event of an exchange, Seller hereby consents to Broker collecting compensation from additional parties for services rendered, provided there is disclosure to all parties of such agency and compensation. Seller understands and agrees that: **(i)** Broker, without the prior written consent of Seller, will not disclose to Buyer that Seller is willing to sell the Property at a price less than the listing price; **(ii)** Broker, without the prior written consent of Buyer, will not disclose to Seller that Buyer is willing to pay a price greater than the offered price; and **(iii)** except for (i) and (ii) above, a dual agent is obligated to disclose known facts materially affecting the value or desirability of the Property to both parties.
    D. **Other Sellers:** Seller understands that Broker may have or obtain listings on other properties, and that potential buyers may consider, make offers on, or purchase through Broker, property the same as or similar to Seller's Property. Seller consents to Broker's representation of sellers and buyers of other properties before, during and after the end of this Agreement.
    E. **Confirmation:** If the Property includes residential property with one-to-four dwelling units, Broker shall confirm the agency relationship described above, or as modified, in writing, prior to or concurrent with Seller's execution of a purchase agreement.
11. **SECURITY AND INSURANCE:** Broker is not responsible for loss of or damage to personal or real property, or person, whether attributable to use of a keysafe/lockbox, a showing of the Property, or otherwise. Third parties, including, but not limited to, appraisers, inspectors, brokers and prospective buyers, may have access to, and take videos and photographs of, the interior of the Property. Seller agrees: **(i)** to take reasonable precautions to safeguard and protect valuables that might be accessible during showings of the Property; and **(ii)** to obtain insurance to protect against these risks. Broker does not maintain insurance to protect Seller.
12. **KEYSAFE/LOCKBOX:** A keysafe/lockbox is designed to hold a key to the Property to permit access to the Property by Broker, cooperating brokers, MLS participants, their authorized licensees and representatives, authorized inspectors, and accompanied prospective buyers. Broker, cooperating brokers, MLS and Associations/Boards of REALTORS® are **not** insurers against injury, theft, loss, vandalism or damage attributed to the use of a keysafe/lockbox. Seller does (or if checked ☐ does not) authorize Broker to install a keysafe/lockbox. If Seller does not occupy the Property, Seller shall be responsible for obtaining occupant(s)' written permission for use of a keysafe/lockbox.
13. **SIGN:** Seller does (or if checked ☐ does not) authorize Broker to install a FOR SALE/SOLD sign on the Property.
14. **EQUAL HOUSING OPPORTUNITY:** The Property is offered in compliance with federal, state and local anti-discrimination laws.
15. **ATTORNEY FEES:** In any action, proceeding or arbitration between Seller and Broker regarding the obligation to pay compensation under this Agreement, the prevailing Seller or Broker shall be entitled to reasonable attorney fees and costs from the non-prevailing Seller or Broker, except as provided in paragraph 19A.
16. **ADDITIONAL TERMS:** _____

Seller acknowledges receipt of a copy of this page.
Seller's Initials (_____)(_____)

Copyright © 1991-2009, CALIFORNIA ASSOCIATION OF REALTORS®, INC.

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

Print

Property Address: _____ Date: _____

17. **MANAGEMENT APPROVAL:** If an associate-licensee in Broker's office (salesperson or broker-associate) enters into this Agreement on Broker's behalf, and Broker or Manager does not approve of its terms, Broker or Manager has the right to cancel this Agreement, in writing, within **5 Days** After its execution.
18. **SUCCESSORS AND ASSIGNS:** This Agreement shall be binding upon Seller and Seller's successors and assigns.
19. **DISPUTE RESOLUTION:**
    A. **MEDIATION:** Seller and Broker agree to mediate any dispute or claim arising between them out of this Agreement, or any resulting transaction, before resorting to arbitration or court action, subject to paragraph 19B(2) below. Paragraph 19B(2) below applies whether or not the arbitration provision is initialed. Mediation fees, if any, shall be divided equally among the parties involved. If, for any dispute or claim to which this paragraph applies, any party commences an action without first attempting to resolve the matter through mediation, or refuses to mediate after a request has been made, then that party shall not be entitled to recover attorney fees, even if they would otherwise be available to that party in any such action. THIS MEDIATION PROVISION APPLIES WHETHER OR NOT THE ARBITRATION PROVISION IS INITIALED.
    B. **ARBITRATION OF DISPUTES: (1) Seller and Broker agree that any dispute or claim in law or equity arising between them regarding the obligation to pay compensation under this Agreement, which is not settled through mediation, shall be decided by neutral, binding arbitration, including and subject to paragraph 19B(2) below. The arbitrator shall be a retired judge or justice, or an attorney with at least 5 years of residential real estate law experience, unless the parties mutually agree to a different arbitrator, who shall render an award in accordance with substantive California law. The parties shall have the right to discovery in accordance with California Code of Civil Procedure §1283.05. In all other respects, the arbitration shall be conducted in accordance with Title 9 of Part III of the California Code of Civil Procedure. Judgment upon the award of the arbitrator(s) may be entered in any court having jurisdiction. Interpretation of this agreement to arbitrate shall be governed by the Federal Arbitration Act.**
    (2) EXCLUSIONS FROM MEDIATION AND ARBITRATION: The following matters are excluded from mediation and arbitration: (i) a judicial or non-judicial foreclosure or other action or proceeding to enforce a deed of trust, mortgage, or installment land sale contract as defined in California Civil Code §2985; (ii) an unlawful detainer action; (iii) the filing or enforcement of a mechanic's lien; and (iv) any matter that is within the jurisdiction of a probate, small claims, or bankruptcy court. The filing of a court action to enable the recording of a notice of pending action, for order of attachment, receivership, injunction, or other provisional remedies, shall not constitute a waiver of the mediation and arbitration provisions.

    "NOTICE: BY INITIALING IN THE SPACE BELOW YOU ARE AGREEING TO HAVE ANY DISPUTE ARISING OUT OF THE MATTERS INCLUDED IN THE 'ARBITRATION OF DISPUTES' PROVISION DECIDED BY NEUTRAL ARBITRATION AS PROVIDED BY CALIFORNIA LAW AND YOU ARE GIVING UP ANY RIGHTS YOU MIGHT POSSESS TO HAVE THE DISPUTE LITIGATED IN A COURT OR JURY TRIAL. BY INITIALING IN THE SPACE BELOW YOU ARE GIVING UP YOUR JUDICIAL RIGHTS TO DISCOVERY AND APPEAL, UNLESS THOSE RIGHTS ARE SPECIFICALLY INCLUDED IN THE 'ARBITRATION OF DISPUTES' PROVISION. IF YOU REFUSE TO SUBMIT TO ARBITRATION AFTER AGREEING TO THIS PROVISION, YOU MAY BE COMPELLED TO ARBITRATE UNDER THE AUTHORITY OF THE CALIFORNIA CODE OF CIVIL PROCEDURE. YOUR AGREEMENT TO THIS ARBITRATION PROVISION IS VOLUNTARY."

    "WE HAVE READ AND UNDERSTAND THE FOREGOING AND AGREE TO SUBMIT DISPUTES ARISING OUT OF THE MATTERS INCLUDED IN THE 'ARBITRATION OF DISPUTES' PROVISION TO NEUTRAL ARBITRATION."

    Seller's Initials _____/_____ **Broker's Initials** _____/_____
20. **ENTIRE AGREEMENT:** All prior discussions, negotiations and agreements between the parties concerning the subject matter of this Agreement are superseded by this Agreement, which constitutes the entire contract and a complete and exclusive expression of their agreement, and may not be contradicted by evidence of any prior agreement or contemporaneous oral agreement. If any provision of this Agreement is held to be ineffective or invalid, the remaining provisions will nevertheless be given full force and effect. This Agreement and any supplement, addendum or modification, including any photocopy or facsimile, may be executed in counterparts.

By signing below, Seller acknowledges that Seller has read, understands, received a copy of and agrees to the terms of this Agreement.

Seller _____ Date _____
Address _____ City _____ State _____ Zip _____
Telephone _____ Fax _____ E-mail _____

Seller _____ Date _____
Address _____ City _____ State _____ Zip _____
Telephone _____ Fax _____ E-mail _____

Real Estate Broker (Firm) _____ DRE Lic. # _____
By (Agent) _____ DRE Lic. # _____ Date _____
Address _____ City _____ State _____ Zip _____
Telephone _____ Fax _____ E-mail _____

THIS FORM HAS BEEN APPROVED BY THE CALIFORNIA ASSOCIATION OF REALTORS® (C.A.R.). NO REPRESENTATION IS MADE AS TO THE LEGAL VALIDITY OR ADEQUACY OF ANY PROVISION IN ANY SPECIFIC TRANSACTION. A REAL ESTATE BROKER IS THE PERSON QUALIFIED TO ADVISE ON REAL ESTATE TRANSACTIONS. IF YOU DESIRE LEGAL OR TAX ADVICE, CONSULT AN APPROPRIATE PROFESSIONAL.
This form is available for use by the entire real estate industry. It is not intended to identify the user as a REALTOR®. REALTOR® is a registered collective membership mark which may be used only by members of the NATIONAL ASSOCIATION OF REALTORS® who subscribe to its Code of Ethics.

Published and Distributed by:
REAL ESTATE BUSINESS SERVICES, INC.
a subsidiary of the California Association of REALTORS®
525 South Virgil Avenue, Los Angeles, California 90020

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

Comment: This form is reprinted with the permission of the California Association of Realtors®. Endorsement is not implied.

© The Regents of the University of California

§2.58 b. Exclusive Agency

An exclusive agency listing provides that the broker is the only agent authorized to procure offers to purchase the property and is entitled to a commission even if another broker sells the property. *Fleming v Dolfin* (1931) 214 C 269, 4 P2d 776; *Carlsen v Zane* (1968) 261 CA2d 399, 67 CR 747. If the owner independently procures a buyer and sells the property, however, the broker is not entitled to the commission. *Faith v Meisetschlager* (1919) 45 CA 7, 187 P 61. But see *Coldwell Banker & Co. v Pepper Tree Office Ctr. Assocs.* (1980) 106 CA3d 272, 165 CR 51, disapproved on other grounds in *Barrett v Bank of America* (1986) 183 CA3d 1362, 1371, 229 CR 16, in which the broker was denied a commission under an exclusive agency listing despite the absence of a finding that the owner was the procuring cause. Most brokers will not accept a listing when the seller reserves the right to sell the property on its own or with other exclusions to the broker's exclusive right to sell.

If the broker presents an offer from a ready, willing, and able buyer before a purchase agreement is executed by a buyer independently procured by the seller, the broker is entitled to the commission. *Houston v Williams* (1921) 53 CA 267, 200 P 55. Conversely, if the seller procures a buyer and enters into a purchase agreement before the broker procures a buyer, the broker's right to the commission is lost. *California Land Sec. Co. v Ritchie* (1919) 40 CA 246, 180 P 625. Sale of the property by the owner automatically terminates an exclusive agency listing, even if the broker is not notified. *E.A. Strout W. Realty v Gregoire* (1950) 101 CA2d 512, 225 P2d 585. If the owner sells to a prospective buyer who had already been contacted by the listing broker, the broker must show that he or she was the procuring cause. *Nelson v Mayer* (1954) 122 CA2d 438, 265 P2d 52. For discussion of procuring cause, see §§2.99-2.105.

As with an exclusive right-to-sell agreement, courts will not find the existence of an exclusive agency in the absence of clear and specific language. *Summers v Freeman* (1954) 128 CA2d 828, 276 P2d 131. An exclusive agency listing must also contain a definite termination date. Bus & P C §10176(f).

© The Regents of the University of California

c. Open Listing

§2.59 (1) General Characteristics

An open (or general) listing requires the broker to be the procuring cause (see §§2.99-2.105) of a buyer who is ready, willing, and able (see §§2.106-2.109) to purchase the property on the terms of the listing. An owner can employ a number of brokers to sell the same property under open listing agreements, and the first broker to procure a buyer earns the commission. *Marks v Rowley* (1951) 102 CA2d 619, 228 P2d 29. If the owner sells the property without a broker's assistance, all open listings are terminated, and no commission is owed. *Edens v Stoddard* (1954) 126 CA2d 56, 271 P2d 610. Unlike either of the exclusive listings, an open listing agreement need not contain a definite termination date. Bus & P C §10176(f); *Summers v Freeman* (1954) 128 CA2d 828, 276 P2d 131. An open listing without a specified duration may be revoked by the owner at any time before the broker produces a buyer, regardless of the efforts the broker may have made before termination. *Tetrick v Sloan* (1959) 170 CA2d 540, 339 P2d 613; *Heffernan v Merrill Estate Co.* (1946) 77 CA2d 106, 174 P2d 710. The only limitation on the owner's right to terminate is that the revocation must be made in good faith. *Tetrick v Sloan, supra*.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.60 (2) Form: Nonexclusive ('Open') Agency Residential Listing Agreement (Authorization and Right to Sell) (CAR Form RLAN)

§2.60 (2) Form: Nonexclusive ("Open") Agency Residential Listing Agreement (Authorization and Right to Sell) (CAR Form RLAN)



CALIFORNIA ASSOCIATION OF REALTORS®

RESIDENTIAL LISTING AGREEMENT - "OPEN"

(Non-Exclusive Authorization and Right to Sell)

(C.A.R. Form RLAN, Revised 4/06)

1. **NON-EXCLUSIVE RIGHT TO SELL:** _____ ("Seller") hereby employs and grants _____ ("Broker") beginning (date) _____ and ending at 11:59 P.M. on (date) _____ ("Listing Period") the non-exclusive and irrevocable right to sell or exchange the real property in the City of _____, County of _____, Assessor's Parcel No. _____, California, described as: _____ ("Property").
2. **ITEMS EXCLUDED AND INCLUDED:** Unless otherwise specified in a real estate purchase agreement, all fixtures and fittings that are attached to the Property are included, and personal property items are excluded, from the purchase price.
ADDITIONAL ITEMS EXCLUDED: _____.
ADDITIONAL ITEMS INCLUDED: _____.
Seller intends that the above items be excluded or included in offering the Property for sale, but understands that: **(i)** the purchase agreement supersedes any intention expressed above and will ultimately determine which items are excluded and included in the sale; and **(ii)** Broker is not responsible for and does not guarantee that the above exclusions and/or inclusions will be in the purchase agreement.
3. **LISTING PRICE AND TERMS:**
   A. The listing price shall be: _____ Dollars ($_____).
   B. Additional Terms: _____.
4. **COMPENSATION TO BROKER:**
Notice: The amount or rate of real estate commissions is not fixed by law. They are set by each Broker individually and may be negotiable between Seller and Broker (real estate commissions include all compensation and fees to Broker).
   A. Seller agrees to pay to Broker as compensation for services irrespective of agency relationship(s), either ☐ _____ percent of the listing price (or if a purchase agreement is entered into, of the purchase price), or ☐ $ _____, AND _____, as follows:
   (1) If during the listing period, or any extension, Broker procures a buyer(s) who offers to purchase the Property on the above price and terms, or any price or terms acceptable to Seller (Broker is entitled to compensation whether any escrow resulting from such offer closes during or after the expiration of the Listing Period).
   OR (2) If within _____ calendar days (a) after the end of the Listing Period or any extension, or (b) after any cancellation of this Agreement, unless otherwise agreed, Seller enters into a contract to sell, convey, lease or otherwise transfer the Property to anyone ("Prospective Buyer") or that person's related entity: **(i)** who physically entered and was shown the Property during the Listing Period or any extension by Broker or a cooperating broker; or **(ii)** for whom Broker or any cooperating broker submitted to Seller a signed, written offer to acquire, lease, exchange or obtain an option on the Property. Seller, however, shall have no obligation to Broker under this paragraph 4A(2) unless, not later than **3 calendar days** after the end of the Listing Period or any extension thereof, Broker has given Seller a written notice of the names of such Prospective Buyers.
   OR (3) If, without Broker's prior written consent, the Property is withdrawn from sale, conveyed, leased, rented, otherwise transferred, or made unmarketable by a voluntary act of Seller during the Listing Period, or any extension, except as specified in paragraph 4G below.
   B. If completion of the sale is prevented by a party to the transaction other than Seller, then compensation due under paragraph 4A shall be payable only if and when Seller collects damages by suit, arbitration, settlement or otherwise, and then in an amount equal to the lesser of one-half of the damages recovered or the above compensation, after first deducting title and escrow expenses and the expenses of collection, if any.
   C. In addition, Seller agrees to pay Broker: _____.
   D. Seller has been advised of Broker's policy regarding cooperation with, and the amount of compensation offered to, other brokers.
   (1) Broker is authorized to cooperate with and compensate brokers participating through the multiple listing service(s) ("MLS"): **(i)** by offering MLS brokers: either ☐ _____ percent of the purchase price, or ☐ $ _____; **OR (ii)** (if checked) ☐ as per Broker's policy.
   (2) Broker is authorized to cooperate with and compensate brokers operating outside the MLS as per Broker's policy.
   E. Seller hereby irrevocably assigns to Broker the above compensation from Seller's funds and proceeds in escrow. Broker may submit this Agreement, as instructions to compensate Broker pursuant to paragraph 4A, to any escrow regarding this Property involving Seller and a buyer, Prospective Buyer or other transferee.
   F. **(1)** Seller represents that Seller has not previously entered into a listing agreement with another broker regarding the Property, unless specified as follows: _____.
   (2) Seller warrants that Seller has no obligation to pay compensation to any other broker regarding the Property unless the Property is transferred to any of the following individuals or entities: _____.
   (3) If the Property is sold to anyone listed above during the time Seller is obligated to compensate another broker: **(i)** Broker is not entitled to compensation under this Agreement; and **(ii)** Broker is not obligated to represent Seller in such transaction.

The copyright laws of the United States (Title 17 U.S. Code) forbid the unauthorized reproduction of this form, or any portion thereof, by photocopy machine or any other means, including facsimile or computerized formats. Copyright © 1991-2006, CALIFORNIA ASSOCIATION OF REALTORS®, INC. ALL RIGHTS RESERVED.

Seller acknowledges receipt of a copy of this page.
Seller's Initials (_____)(_____)

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

Print

Property Address: _____ Date: _____

G. This is a non-exclusive agency listing. Seller reserves the right to sell the Property either directly to a purchaser, or through another broker, without any obligation to pay compensation to Broker, unless otherwise specified in paragraph 4C above or elsewhere in writing.

5. **OWNERSHIP, TITLE AND AUTHORITY:** Seller warrants that: **(i)** Seller is the owner of the Property, **(ii)** no other persons or entities have title to the Property; and **(iii)** Seller has the authority to both execute this Agreement and sell the Property. Exceptions to ownership, title and authority are as follows: _____.
6. **MULTIPLE LISTING SERVICE:** All terms of the transaction, including financing, if applicable, will be provided to the selected MLS for publication, dissemination and use by persons and entities on terms approved by the MLS. Seller authorizes Broker to comply with all applicable MLS rules. MLS rules allow MLS data to be made available by the MLS to additional Internet sites unless Broker gives the MLS instructions to the contrary. MLS rules generally provide that residential real property and vacant lot listings be submitted to the MLS within 48 hours or some other period of time after all necessary signatures have been obtained on the listing agreement. However, Broker will not have to submit this listing to the MLS if, within that time, Broker submits to the MLS a form signed by Seller (C.A.R. Form SEL or the locally required form) instructing Broker to withhold the listing from the MLS. Information about this listing will be provided to the MLS of Broker's selection unless a form instructing Broker to withhold the listing from the MLS is attached to this listing Agreement.
7. **SELLER REPRESENTATIONS:** Seller represents that, unless otherwise specified in writing, Seller is unaware of: **(i)** any Notice of Default recorded against the Property; **(ii)** any delinquent amounts due under any loan secured by, or other obligation affecting, the Property; **(iii)** any bankruptcy, insolvency or similar proceeding affecting the Property; **(iv)** any litigation, arbitration, administrative action, government investigation or other pending or threatened action that affects or may affect the Property or Seller's ability to transfer it; and **(v)** any current, pending or proposed special assessments affecting the Property. Seller shall promptly notify Broker in writing if Seller becomes aware of any of these items during the Listing Period or any extension thereof.
8. **BROKER'S AND SELLER'S DUTIES:** Broker agrees to exercise reasonable effort and due diligence to achieve the purposes of this Agreement. Unless Seller gives Broker written instructions to the contrary, Broker is authorized to order reports and disclosures as appropriate or necessary and advertise and market the Property by any method and in any medium selected by Broker including MLS and the Internet, and, to the extent permitted by these media, control the dissemination of the information submitted to any medium. Seller agrees to consider offers presented by Broker, and to act in good faith to accomplish the sale of the Property by, among other things, making the Property available for showing at reasonable times and referring to Broker all inquiries of any party interested in the Property. Seller is responsible for determining at what price to list and sell the Property. **Seller further agrees to indemnify, defend and hold Broker harmless from all claims, disputes, litigation, judgments and attorney fees arising from any incorrect information supplied by Seller, or from any material facts that Seller knows but fails to disclose.**
9. **DEPOSIT:** Broker is authorized to accept and hold on Seller's behalf any deposits to be applied toward the purchase price.
10. **AGENCY RELATIONSHIPS:**
    A. **Disclosure:** If the Property includes residential property with one-to-four dwelling units, Seller shall receive a "Disclosure Regarding Agency Relationships" (C.A.R. Form AD) form prior to entering into this Agreement.
    B. **Seller Representation:** Broker shall represent Seller in any resulting transaction, except as specified in paragraph 4F.
    C. **Possible Dual Agency With Buyer:** Depending upon the circumstances, it may be necessary or appropriate for Broker to act as an agent for both Seller and buyer, exchange party, or one or more additional parties ("Buyer"). Broker shall, as soon as practicable, disclose to Seller any election to act as a dual agent representing both Seller and Buyer. If a Buyer is procured directly by Broker or an associate-licensee in Broker's firm, Seller hereby consents to Broker acting as a dual agent for Seller and such Buyer. In the event of an exchange, Seller hereby consents to Broker collecting compensation from additional parties for services rendered, provided there is disclosure to all parties of such agency and compensation. Seller understands and agrees that: **(i)** Broker, without the prior written consent of Seller, will not disclose to Buyer that Seller is willing to sell the Property at a price less than the listing price; **(ii)** Broker, without the prior written consent of Buyer, will not disclose to Seller that Buyer is willing to pay a price greater than the offered price; and **(iii)** except for (i) and (ii) above, a dual agent is obligated to disclose known facts materially affecting the value or desirability of the Property to both parties.
    D. **Other Sellers:** Seller understands that Broker may have or obtain listings on other properties, and that potential buyers may consider, make offers on, or purchase through Broker, property the same as or similar to Seller's Property. Seller consents to Broker's representation of sellers and buyers of other properties before, during and after the end of this Agreement.
    E. **Confirmation:** If the Property includes residential property with one-to-four dwelling units, Broker shall confirm the agency relationship described above, or as modified, in writing, prior to or concurrent with Seller's execution of a purchase agreement.
11. **SECURITY AND INSURANCE:** Broker is not responsible for loss of or damage to personal or real property, or person, whether attributable to use of a keysafe/lockbox, a showing of the Property, or otherwise. Third parties, including but not limited to, appraisers, inspectors, brokers and prospective buyers, may have access to, and take videos and photographs of, the interior of the Property. Seller agrees: **(i)** to take reasonable precautions to safeguard and protect valuables that might be accessible during showings of the Property; and **(ii)** to obtain insurance to protect against these risks. Broker does not maintain insurance to protect Seller.
12. **KEYSAFE/LOCKBOX:** A keysafe/lockbox is designed to hold a key to the Property to permit access to the Property by Broker, cooperating brokers, MLS participants, their authorized licensees and representatives, authorized inspectors, and accompanied prospective buyers. Broker, cooperating brokers, MLS and Associations/Boards of REALTORS® are **not** insurers against injury, theft, loss, vandalism or damage attributed to the use of a keysafe/lockbox. Seller does (or if checked ☐ does not) authorize Broker to install a keysafe/lockbox. If Seller does not occupy the Property, Seller shall be responsible for obtaining occupant(s)' written permission for use of a keysafe/lockbox.
13. **SIGN:** Seller does (or if checked ☐ does not) authorize Broker to install a FOR SALE/SOLD sign on the Property.
14. **EQUAL HOUSING OPPORTUNITY:** The Property is offered in compliance with federal, state and local anti-discrimination laws.
15. **ATTORNEY FEES:** In any action, proceeding or arbitration between Seller and Broker regarding the obligation to pay compensation under this Agreement, the prevailing Seller or Broker shall be entitled to reasonable attorney fees and costs, except as provided in paragraph 19A.
16. **ADDITIONAL TERMS:** _____

_____

_____

_____

Seller acknowledges receipt of a copy of this page.
Seller's Initials (_____)(_____)

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

Copyright © 1991-2006, CALIFORNIA ASSOCIATION OF REALTORS®, INC.

Print

Property Address: _____ Date: _____

17. **MANAGEMENT APPROVAL:** If an associate-licensee in Broker's office (salesperson or broker-associate) enters into this listing Agreement on Broker's behalf, and Broker or Manager does not approve of its terms, Broker or Manager has the right to cancel this Agreement, in writing, within **5 Days** After its execution.
18. **SUCCESSORS AND ASSIGNS:** This Agreement shall be binding upon Seller and Seller's successors and assigns.
19. **DISPUTE RESOLUTION:**
    A. **MEDIATION:** Seller and Broker agree to mediate any dispute or claim arising between them out of this Agreement, or any resulting transaction, before resorting to arbitration or court action, subject to paragraph 19B(2) below. Paragraph 19B(2) below applies whether or not the arbitration provision is initialed. Mediation fees, if any, shall be divided equally among the parties involved. If for any dispute or claim to which this paragraph applies, any party commences an action without first attempting to resolve the matter through mediation, or refuses to mediate after a request has been made, then that party shall not be entitled to recover attorney fees, even if they would otherwise be available to that party in any such action. THIS MEDIATION PROVISION APPLIES WHETHER OR NOT THE ARBITRATION PROVISION IS INITIALED.
    B. **ARBITRATION OF DISPUTES: (1) Seller and Broker agree that any dispute or claim in law or equity arising between them regarding the obligation to pay compensation under this Agreement, which is not settled through mediation, shall be decided by neutral, binding arbitration, including and subject to paragraph 19B(2) below. The arbitrator shall be a retired judge or justice, or an attorney with at least 5 years of residential real estate law experience, unless the parties mutually agree to a different arbitrator, who shall render an award in accordance with substantive California law. The parties shall have the right to discovery in accordance with Code of Civil Procedure §1283.05. In all other respects, the arbitration shall be conducted in accordance with Title 9 of Part III of the California Code of Civil Procedure. Judgment upon the award of the arbitrator(s) may be entered in any court having jurisdiction. Interpretation of this agreement to arbitrate shall be governed by the Federal Arbitration Act.**
    (2) EXCLUSIONS FROM MEDIATION AND ARBITRATION: The following matters are excluded from mediation and arbitration: (i) a judicial or non-judicial foreclosure or other action or proceeding to enforce a deed of trust, mortgage, or installment land sale contract as defined in Civil Code §2985; (ii) an unlawful detainer action; (iii) the filing or enforcement of a mechanic's lien; and (iv) any matter that is within the jurisdiction of a probate, small claims, or bankruptcy court. The filing of a court action to enable the recording of a notice of pending action, for order of attachment, receivership, injunction, or other provisional remedies, shall not constitute a waiver of the mediation and arbitration provisions.

    "NOTICE: BY INITIALING IN THE SPACE BELOW YOU ARE AGREEING TO HAVE ANY DISPUTE ARISING OUT OF THE MATTERS INCLUDED IN THE 'ARBITRATION OF DISPUTES' PROVISION DECIDED BY NEUTRAL ARBITRATION AS PROVIDED BY CALIFORNIA LAW AND YOU ARE GIVING UP ANY RIGHTS YOU MIGHT POSSESS TO HAVE THE DISPUTE LITIGATED IN A COURT OR JURY TRIAL. BY INITIALING IN THE SPACE BELOW YOU ARE GIVING UP YOUR JUDICIAL RIGHTS TO DISCOVERY AND APPEAL, UNLESS THOSE RIGHTS ARE SPECIFICALLY INCLUDED IN THE 'ARBITRATION OF DISPUTES' PROVISION. IF YOU REFUSE TO SUBMIT TO ARBITRATION AFTER AGREEING TO THIS PROVISION, YOU MAY BE COMPELLED TO ARBITRATE UNDER THE AUTHORITY OF THE CALIFORNIA CODE OF CIVIL PROCEDURE. YOUR AGREEMENT TO THIS ARBITRATION PROVISION IS VOLUNTARY."

    "WE HAVE READ AND UNDERSTAND THE FOREGOING AND AGREE TO SUBMIT DISPUTES ARISING OUT OF THE MATTERS INCLUDED IN THE 'ARBITRATION OF DISPUTES' PROVISION TO NEUTRAL ARBITRATION."

    Seller's Initials _____/_____ **Broker's Initials** _____/_____
20. **ENTIRE AGREEMENT:** All prior discussions, negotiations and agreements between the parties concerning the subject matter of this agreement are superseded by this Agreement, which constitutes the entire contract and a complete and exclusive expression of their agreement, and may not be contradicted by evidence of any prior agreement or contemporaneous oral agreement. If any provision of this Agreement is held to be ineffective or invalid, the remaining provisions will nevertheless be given full force and effect. This Agreement and any supplement, addendum or modification, including any photocopy or facsimile, may be executed in counterparts.

By signing below, Seller acknowledges that Seller has read, understands, received a copy of and agrees to the terms of this Agreement.

Seller _____ Date _____
Address _____ City _____ State _____ Zip _____
Telephone _____ Fax _____ E-mail _____

Seller _____ Date _____
Address _____ City _____ State _____ Zip _____
Telephone _____ Fax _____ E-mail _____

Real Estate Broker (Firm) _____ DRE Lic. # _____
By (Agent) _____ DRE Lic. # _____ Date _____
Address _____ City _____ State _____ Zip _____
Telephone _____ Fax _____ E-mail _____

THIS FORM HAS BEEN APPROVED BY THE CALIFORNIA ASSOCIATION OF REALTORS® (C.A.R.). NO REPRESENTATION IS MADE AS TO THE LEGAL VALIDITY OR ADEQUACY OF ANY PROVISION IN ANY SPECIFIC TRANSACTION. A REAL ESTATE BROKER IS THE PERSON QUALIFIED TO ADVISE ON REAL ESTATE TRANSACTIONS. IF YOU DESIRE LEGAL OR TAX ADVICE, CONSULT AN APPROPRIATE PROFESSIONAL.
This form is available for use by the entire real estate industry. It is not intended to identify the user as a REALTOR®. REALTOR® is a registered collective membership mark which may be used only by members of the NATIONAL ASSOCIATION OF REALTORS® who subscribe to its Code of Ethics.

SURE TRAC The System for Success®
Published and Distributed by:
REAL ESTATE BUSINESS SERVICES, INC.
a subsidiary of the California Association of REALTORS®
525 South Virgil Avenue, Los Angeles, California 90020

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

SAMPLE

Comment: This form is reprinted with the permission of the California Association of Realtors®. Endorsement is not implied.

© The Regents of the University of California

§2.61 d. Net Listing Provisions

Under a net listing provision, the broker's commission is earned in any manner the parties agree on (*e.g.,* any one of the listing agreements in §§2.56-2.60), but the amount of the commission is the amount by which the actual sale price exceeds a stated net price to the seller. See *Smith v Zak* (1971) 20 CA3d 785, 98 CR 242; §2.132. If the property is sold for the specified net sum or a lesser amount, the broker does not earn a commission. *Haigler v Donnelly* (1941) 18 C2d 674, 117 P2d 331. Although legal, a net listing provision provides an obvious opportunity for abuse by brokers, and its use will be scrutinized closely by the Real Estate Commissioner under the authority of Bus & P C §10176(g).

Both brokers and owners should be cautious about using net listing arrangements. A broker should explain the nature and effect of a net listing to the principal and should make sure that the net sale price is set by the owner. Any facts tending to indicate that the broker influenced the price may subject the broker to liability for secret profits (see §§2.139, 2.160) and disciplinary action by the Real Estate Commissioner (see §2.171).

A broker must ordinarily disclose to the seller any amounts he or she will receive as a result of the sale (see §§2.139, 2.160) and any interest, direct or indirect, the broker has in the purchase of the property (see §§2.137-2.141). There is some authority for easing these disclosure requirements when the property is sold under a net listing (*Pascal v Cotton* (1962) 205 CA2d 597, 23 CR 357; see §2.138), but the continuing vitality of this exception is open to question and, in any event, it is strictly limited to sales in which the net price was set by the seller without any influence from the broker. *Sierra Pac. Indus. v Carter* (1980) 104 CA3d 579, 163 CR 764. Courts have held the broker to a strict duty to disclose when the broker has influenced the setting of the net price. *Sierra Pac. Indus. v Carter, supra*.

© The Regents of the University of California

§2.62 3. Forms and Provisions for Listing Agreements

The listing agreement may be prepared in any format acceptable to the seller and the broker. The Residential Listing Agreement (Exclusive Authorization and Right to Sell) published by the California Association of Realtors® is set forth in §2.57. Most standard listing agreements tend to favor brokers, and the seller's attorney should make any changes or include any additional provisions on an addendum or rider attached to the listing agreement. See §2.55 for a checklist of what to review. Alternatively, the attorney may prefer to draft the listing agreement either in the form of a letter agreement employing the broker or in a formally prepared and executed employment contract.

Circumstances will dictate the format to use in a given transaction. Brokers (especially residential brokers) usually prefer their own forms and more readily accept riders to those forms. Using a rider presents some risk of contradiction between the agreement and the rider, and both should be carefully reviewed for consistency. The form agreement should include a notation that it is subject to the attached rider. The seller and the broker should initial the notation and sign the addendum.

The form provisions in §§2.64-2.88 are intended to enable the seller's attorney to draft a complete listing agreement, letter agreement, or rider to a standard form agreement. Some of the provisions are found in standard listing agreements; others are generally omitted from standard agreements but should be added by addendum or separate agreement when needed by the parties. Many of the provisions are not essential to every listing agreement, but they could be useful to cover a situation in a particular transaction.

The seller's attorney, whether using a standard form listing agreement or an attorney-drafted form, should carefully review or draft each provision, paying special attention to the provision specifying when the commission is earned and the other provisions discussed in §§2.63-2.88.

© The Regents of the University of California

a. Termination Date

§2.63 (1) Need for Definite Date

An exclusive agency or right-to-sell listing agreement must contain a definite termination date for the listing period. See §§2.56-2.58. A broker is subject to discipline under Bus & P C §10176(f) for attempting to collect compensation under either of these exclusive listings if it does not have a termination date. The broker who has performed fully under an exclusive listing agreement without a termination date may, however, be able to recover the commission if the seller has benefited from those services. See *Babcock v Houston* (1973) 33 CA3d 858, 109 CR 454 (transaction was completed, no serious moral turpitude was involved, defendant was guilty of greatest moral fault, and applying rule would give unjust enrichment). *Schaffter v Creative Capital Leasing Group, LLC* (2008) 166 CA4th 745, 752, 83 CR3d 19 (argument that commission agreement was unenforceable because it lacked definite termination date was waived when defendant failed to notify broker of issue). If the broker has not performed, the owner can rescind the agreement and the broker cannot enforce it. *Nichols v Boswell-Alliance Constr. Corp.* (1960) 181 CA2d 584, 5 CR 546.

The termination date need not be a calendar date, but it must be determinable from the listing agreement itself without reference to some external event. *Dale v Palmer* (1951) 106 CA2d 663, 235 P2d 650. Listing agreements that provide for the listing to continue until revoked by the seller, but in no event later than a definite calendar date, have been upheld. See *Lowe v Loyd* (1949) 93 CA2d 684, 209 P2d 851. A listing that purported to renew automatically after a period of time, unless actively terminated by the seller, would not be enforceable. *Dale v Palmer, supra*.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.64 (2) Form: Listing Period

§2.64 (2) Form: Listing Period

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§2.64-2.88.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

2.64-1 Employment of broker

[*Add one of the following alternatives*]

[*Alternative 1: Letter agreement*]

_ _[*Date*]_ _

_ _[*Name and address of broker*]_ _

Dear _ _[*name*]_ _**:**

_ _[*I/We*]_ _ **employ you as broker**

[*Alternative 2: Employment contract*]

_ _[*Date*]_ _

_ _[*I/We*]_ _ **employ** _ _[*name of broker*]_ _ **as broker**

[*Continue*]

for the period beginning _ _[*date*]_ _**, and ending at midnight on** _ _[*date*]_ _**, called the listing period, for the sale of** _ _[*my/our*]_ _ _ _[*specify, e.g., fee interest/undivided interest/leasehold interest/fee interest subject to leasehold*]_ _ **in the real property in the City of** _ _[*name*]_ _**, County of** _ _[*name*]_ _**, described as follows:** _ _[*describe property by address, legal description, assessor's parcel number, or other appropriate means*]_ _**.**

Comment: The need to use language indicating the broker's employment is discussed in §2.45. Most standard agreements specify at the beginning the type of listing agreement that the broker is employed under (open, exclusive agency, or exclusive right-to-sell listing). These specifications actually define the conditions under which the commission is earned, so they should also be included in the provision on the broker's commission. See the form provision in §2.79.

The event triggering the broker's right to a commission must occur during the term of the listing or an agreed-upon extension. This event is usually the formation of a contract between the buyer and the seller that ultimately leads to a closed transaction. Close of escrow, which may dictate *when* the commission is due or may be a condition to payment of the commission, may occur *after* the term has ended. Although listing agreements are commonly granted for a specific number of days or months, a specific termination date is recommended for clarity. For a further discussion of the termination date, see §2.63.

The Statute of Frauds does not require that the listing agreement contain an exact legal description of the property as long as the description adequately identifies the property. CC §1624(a); see §2.46. Whether a street address, legal description, or assessor's parcel number is used, accuracy is vital. The purchase agreement will probably describe the property as it is shown in the listing agreement, and the buyer may have a defense against performing if the description in the purchase agreement is not correct. See California Real Property Remedies and Damages §4.19 (2d ed Cal CEB 2002) on the uncertainty of a legal description as a defense to the enforcement of the purchase agreement.

© The Regents of the University of California

b. Listing Price

§2.65 (1) Negotiating Listing Price; Method of Payment

To meet the seller's objectives and be competitively priced, the listing price should be the product of discussion and negotiation between the broker and the seller. Occasionally, brokers overstate the value of the property to obtain the listing and eliminate competition. This practice is unethical and may subject the broker to discipline. See Bus & P C §§10176-10177. Moreover, brokers should avoid the pitfall of overstating the value to indulge a seller who is not committed to selling the property at a realistic market price.

The broker earns the commission by producing a buyer who can pay cash. See §§2.106-2.109 on when the commission is earned. If the seller is willing to accept some other arrangement for all or part of the purchase price, such as the buyer's note or the buyer's assumption of an existing loan, the listing agreement should specify that the price may be paid by alternative methods. This expands the circumstances under which a broker will have earned a commission even if the seller refuses to sell. More importantly, to market the property effectively, the broker should understand what terms the seller is willing to entertain. See §2.106; see chap 9 on financing terms in the purchase and sale agreement. Most often, these details can be left to the seller and a potential buyer to negotiate.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.66 (2) Form: Listing Price

§2.66 (2) Form: Listing Price

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§2.64-2.88.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

2.66-1 Listing price

[*Add one of the following alternatives*]

[*Alternative 1: Minimum total price*]

The minimum price for sale of the property shall be _ _[*dollar amount*]**_ _ paid as follows: _ _**[*specify, e.g., all cash to seller/in installments as follows: _ _*[*specify installments*]*_ _/(other consideration)*]**_ _.**

[*Alternative 2: Net price to seller*]

The price of the property shall not be less than _ _[*dollar amount*]**_ _ net to seller after deduction of all expenses and costs of sale payable by the seller, except _ _**[*specify expenses seller will bear*]**_ _.**

Comment: Unless the seller requires the transaction to be structured as an installment sale or an exchange, the listing agreement generally need not specify the payment terms in any greater detail than "cash to seller." If the seller wishes the transaction to be an installment sale under IRC §453, the listing agreement should specify the maximum downpayment the seller will accept, the amounts of future installments, their payment dates, and the interest rate. See chap 9 on installment sales.

Occasionally, the seller may want to specify details of payment of the purchase price in the listing agreement, and the form can be modified for that purpose. In most circumstances, this clause can be used in an exchange without modification if the seller intends the disposition of the property to be the first leg of a tax-deferred exchange (except in the unlikely event such exchange is intended to be direct (*i.e.,* in exchange for the buyer's property) or simultaneous). Because cash is typically generated from the buyer of the taxpayer's property, the broker's commission can usually be paid from the leg of the transaction that generates the cash. See generally Real Property Exchanges (3d ed Cal CEB 2002).

For discussion of net listings, see §2.61.

© The Regents of the University of California

c. Buyer's Deposit

§2.67 (1) Broker Holding Buyer's Deposit

In most localities, by custom and practice escrow agents rather than brokers hold the buyer's deposit. Parties, however, may disagree on who should hold the deposit: an escrow company, the broker, or the seller. An escrow holder may be unsatisfactory because, in a dispute between the buyer and the seller, it will almost invariably refuse to release the deposit to either party unless all parties sign written release instructions, preferring to interplead the funds in the buyer-seller litigation. Custody of the deposit by the broker or the seller exposes the buyer (or seller, see §2.62) to the risk of loss or misappropriation by the other. Brokers are often reluctant to hold funds because of the complex rules on broker trust accounts. See Bus & P C §10145; 10 Cal Code Regs §§2830.1-2836, 2950-2951.

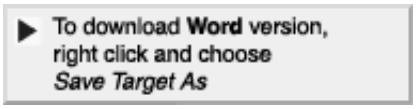
If the broker will hold a deposit, the listing agreement must address the broker's authorization to do so. An express authorization to accept the deposit for the seller renders the broker the seller's agent in holding the deposit, which shifts the risk of loss of the deposit to the seller. *Hicks v Wilson* (1925) 197 C 269, 240 P 289; *Warshauer v Bauer Constr. Co.* (1960) 179 CA2d 44, 3 CR 570. Without express authorization, the broker holds the deposit as the buyer's agent and the buyer retains the risk of loss. *Clark v Patterson* (1931) 213 C 4, 300 P 967. On the broker's duty to account for funds held, see §2.149.

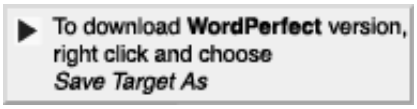
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.68 (2) Form: Authority to Accept Deposits

§2.68 (2) Form: Authority to Accept Deposits

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§2.64-2.88.





2.68-1 Authority to accept deposits

[*If applicable, add one or both of the following options*]

[*Option 1: Authority to Accept Deposit Only as Seller's/Buyer's Agent*]

You are authorized on seller's behalf to accept and hold buyer's deposit. On seller's acceptance of buyer's offer, you are instructed to _ _[*e.g., deliver the deposit to seller/place buyer's deposit in escrow*]**_ _.**

[*Option 2: Authority to accept deposit only as buyer's agent*]

You are authorized to accept buyer's deposit only as buyer's agent until seller's acceptance. The deposit is to be considered accepted only when seller accepts buyer's offer.

Comment: Generally, escrow agents—not brokers—hold the buyer's deposit. See discussion in §2.67. This provision, therefore, generally would not be necessary. If the parties do elect to have the broker hold the deposit, however, this type of provision clarifies for whose benefit the broker holds the deposit. The issue of for whose benefit the broker holds the deposit is affected by the type of agency relationship that the broker and the seller confirm before execution of the listing. See §§2.31-2.37. If the seller and the broker agree that the broker will be a dual agent, the clause in Option 2 above should be used to limit the seller's exposure regarding the deposit. This provision will protect the seller from the broker's loss or misappropriation of the deposit.

© The Regents of the University of California

§2.69 (3) Handling Deposits

When the deposit is deemed paid can depend on the method of payment and intent of the parties. If both the buyer and the seller intend a check to be held as the deposit without being cashed, the broker's receipt of the check will be treated as payment of the deposit. *Beazell v Kane* (1954) 127 CA2d 593, 274 P2d 224. If it is not expressly agreed that the check is to be held without being cashed, the check does not constitute payment of the deposit until it is honored by the drawee bank. *Mendiondo v Greitman* (1949) 93 CA2d 765, 209 P2d 817.

Whatever methods of payment and custody of the deposit are used, the deposit never becomes the property of the broker. The broker holds the deposit as agent, escrow holder, and trustee for the respective parties. *Savage v Mayer* (1949) 33 C2d 548, 203 P2d 9; *Holloway v Thiele* (1953) 116 CA2d 68, 253 P2d 131.

© The Regents of the University of California

§2.70 (4) Form: Handling Deposits

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§2.64-2.88.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

2.70-1 Handling deposits

Buyer's deposit shall be made only _ _[*e.g., in cash or cashier's check or a combination*]**_ _. All checks must be made to the order of _ _**[*e.g., seller/name of escrow holder*]**_ _, and all deposits must be delivered by broker to _ _**[*e.g., seller/escrow holder*]**_ _ by the next business day following receipt.**

Comment: Lawyers frequently require that payments be made in cash or by cashier's check because payment on personal checks, even certified checks, can be stopped. See §4.37. If payment on a check is stopped, both parties may be unsure of their rights regarding the property until the dispute over the check is resolved, and the effect may be to remove the property from the market for a considerable period.

This provision requires immediate delivery of any deposit, which is in the best interest of both the seller and broker. It minimizes the chances for loss or misappropriation by the broker and reduces the time in which the buyer might regret making an offer and decide to stop payment. The broker is required to place the deposit into a neutral escrow depository or broker's trust account no later than 3 business days after receipt. Bus & P C §10145; 10 Cal Code Regs §2832. The buyer retains title to the deposit and is entitled to its return until the seller unconditionally accepts the offer. *Norris v San Mateo County Title Co.* (1951) 37 C2d 269, 231 P2d 493.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/ d. Escrow Holder/§2.71 (1) Selection of Escrow Holder

d. Escrow Holder

§2.71 (1) Selection of Escrow Holder

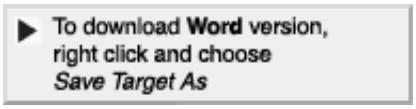
Sellers may wish to designate a particular escrow holder in the listing agreement. The seller's right to select the escrow holder is constrained by CC §2995, which bars a developer from requiring use of an escrow holder in which it has a financial interest, and by the Real Estate Settlement Procedures Act of 1974 (RESPA) (12 USC §§2601-2617), which prohibits most sellers from conditioning the sale on the use of a particular title company (12 USC §2608).

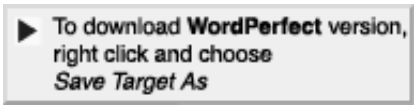
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.72 (2) Form: Designating Escrow Holder

§2.72 (2) Form: Designating Escrow Holder

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§2.64-2.88.





2.72-1 Designating escrow holder

Escrow shall be opened with _ _[*name and address of escrow holder*]_ _, and shall close no sooner than _ _[*date*]_ _, and no later than _ _[*date*]_ _. Broker shall deliver any deposits broker holds under the terms of this listing agreement to the escrow holder on execution by both buyer and seller of a purchase and sale agreement.

Comment: Whether or not an escrow holder is named, the seller may wish to set out the closing date to prevent closing before possession can be delivered in order to ensure that closing occurs by a particular date or to specify a closing date in a particular tax year. On prohibitions on the seller selecting the escrow holder, see §2.71.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.73 e. Form: Possession

§2.73 e. Form: Possession

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§2.64-2.88.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

2.73-1 Possession

Buyer shall have possession of the property _ _[*e.g., at close of escrow/no sooner than* _ _[*date*]_ _]_ _**.**

Comment: If the date of delivery of possession is important to the seller, it should be a condition of the listing agreement. Close of escrow is usually given as the time for delivering possession, but an owner-occupant may need more time to move. Unless given additional time to vacate, an owner who is unable to deliver possession at the close of escrow may be in violation of the purchase agreement.

© The Regents of the University of California

f. Multiple Listing Services

§2.74 (1) Use of MLS

Most residential sellers prefer to use the Multiple Listing Service (MLS) for maximum market exposure, fastest sale, and highest price. It may be a breach of the broker's fiduciary duty to persuade the seller to keep the listing out of the MLS. On broker's fiduciary duties, see §§2.124-2.126; 2 Miller & Starr, California Real Estate §5:32 (3d ed 2000). If the use of a multiple listing service is mandatory, subscribing brokers will be required by the terms of the MLS to submit all their listings or submit a waiver of the MLS signed by the seller.

Some localities have an MLS that will accept commercial listings as well as residential, but they are not generally used for commercial transactions. If used, the listing should address whether the listing broker is required to cooperate (*i.e.,* share its commission) with outside brokers. Sellers often will insist on cooperation and a 50/50 commission split. There are, however, situations in which the seller agrees to some other arrangement (*e.g.,* no cooperation required during first week or two of listing); and in some markets, the listing agreement may customarily provide only for the listing broker's compensation and the buyer's agent must obtain compensation from its own client. In any event, both broker and seller would be served by a clear written expression of their understanding.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.75 (2) Form: Broker Cooperation; Submitting Listing to MLS

§2.75 (2) Form: Broker Cooperation; Submitting Listing to MLS

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§2.64-2.88.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

2.75-1 Broker cooperation; submitting listing to MLS

[*If applicable, add one or both of the following options*]

[*Option 1: Residential*]

Broker _ _[*may/will*]**_ _ refer the listing to the _ _**[*name*]**_ _ multiple listing service and is authorized to cooperate with and compensate any of its members in securing a purchaser.**

[*Option 2: Commercial*]

Broker _ _[*may/will*]**_ __cooperate with other brokers in the marketing and sale of the property _ _**[*from the outset/after the first _ _*[*number*]*_ _ days*]*_ _* **of the listing period _ _**[*and shall share its commission equally with any broker procuring a buyer*]*_ _***.**

Comment: It could be argued that reference to the MLS is authorized when that conforms with local practice, even if the listing agreement is silent. The broker may want to attempt to sell the property without the services of a cooperating broker to avoid having to split the commission, but may also want to retain the right to submit the listing to the MLS, if necessary. The provision on using an MLS can be either permissive or mandatory.

© The Regents of the University of California

g. Broker's Compensation

§2.76 (1) Conditioned on Closing

Whichever type of listing is used, the seller should try to negotiate for payment of the commission only if the sale is consummated. On conditional commission provisions, see §§2.110-2.113. On the differences among open listings, exclusive listings, and exclusive right-to-sell listings, see §§2.56-2.60; on net listings, see §2.61. Specific language that conditions payment on the closing actually occurring is preferable to the more common clauses providing that the commission is "payable" on or at close of escrow. Otherwise, the seller may be liable for the commission if the broker produces a buyer who makes an unconditional offer accepted by the seller, whether or not procured under the listing terms and regardless of whether the sale is consummated. See §§2.106-2.109.

When payment of the commission is conditioned on closing, the seller cannot avoid payment by unreasonably preventing the closing and will be liable for the payment if the failure to close arose from the seller's lack of good faith. *Stromer v Browning* (1966) 65 C2d 421, 55 CR 18; *Seck v Foulks* (1972) 25 CA3d 556, 102 CR 170. See §2.114. Nevertheless, the broker should attempt to negotiate inclusion of explicit language to this effect at the end of the commission-on-closing clause (*e.g.,* commission is earned if closing prevented by seller's default).

© The Regents of the University of California

§2.77 (2) Not Conditioned on Closing

If the commission is not to be conditioned on closing, the seller may wish to provide that, in the event of the buyer's breach, the commission will be limited to half of any damages the seller recovers, not to exceed the agreed commission amount. Language in this form is similar to that in the California Association of Realtors® Residential Purchase Agreement and Joint Escrow Instructions. See §6.24. The purchase agreement may contain such a provision even if the listing agreement does not, in which event the purchase agreement controls (provided that the broker is a party to that agreement), despite the commission provision in the listing agreement. This contract term is not always favorable to the broker. If the amount retained or recovered by the seller is nominal, the broker's recovery may be an inconsequential amount, regardless of any other theory of recovery the broker may have had. *Chapman v Gilmore* (1963) 221 CA2d 506, 34 CR 515.

© The Regents of the University of California

§2.78 (3) Payment From Deposits

Frequently, the only amount really at issue as damages is the deposit, and the seller's right to retain the deposit is governed by statutes on liquidated damages. CC §§1671-1681. If the purchase agreement contains a valid liquidated damages provision and either the listing or purchase agreement provides that the broker shall recover half of any funds recovered by the seller, then the broker is entitled to half of the deposit.

An interesting question arises when the seller elects to return a deposit to which the seller is or may be entitled. Does the provision entitling the broker to half of any funds recovered by the seller entitle the broker to a commission equal to half of the deposit? In *Kritt v Athens Hills Dev. Co.* (1952) 109 CA2d 642, 241 P2d 606, the listing agreement provided that the commission should be one-half of any deposit retained, but it did not obligate the seller to retain the deposit. It was held that the seller had no obligation to retain deposits to which it was otherwise entitled, and the broker recovered nothing for sales on which deposits were returned.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.79 (4) Form: Entitlement to Commission

§2.79 (4) Form: Entitlement to Commission

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§2.64-2.88.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

2.79-1 Entitlement to commission

Seller agrees to pay broker as a commission

[*Add one of the following alternatives*]

[*Alternative 1: Simple percentage*]

_ _[*number*]**_ _ percent of the first _ _**[*dollar amount*]**_ _ of the gross selling price plus _ _**[*number*]**_ _ percent of the gross selling price in excess of _ _**[*dollar amount*]**_ _, if, during the listing period or any extension of it,**

[*Alternative 2: Flat fee*]

the total sum of _ _[*dollar amount*]**_ _ regardless of the selling price _ _**[*or the type or value of any property accepted in exchange for the property*]**_ _, if, during the listing period or any extension of it,**

[*Alternative 3: Balance over net price to seller*]

the balance of the selling price in excess of _ _[*dollar amount*]**_ _ net to seller after payment of all other costs in escrow except the following, which shall be paid by seller out of seller's net price: _ _**[*list expenses to be paid by seller*]**_ _, if, during the listing period or any extension of it,**

[*Continue*]

[*Add one of the following alternative circumstances under which the commission is earned*]

[*Alternative 1: Open listing*]

broker procures a buyer on the terms stated in this listing agreement or any other terms acceptable to seller.

[*Alternative 2: Exclusive agency listing*]

any broker procures a buyer on the terms stated in this listing agreement or any other terms acceptable to seller.

[*Alternative 3: Exclusive right-to-sell listing*]

anyone (including seller) procures a buyer on the terms stated in this listing agreement or any other terms acceptable to seller.

[*Continue*]

[*If applicable, add one or more of the following options*]

[*Option 1: Commission conditioned on closing or seller's default*]

Payment of the commission shall be conditioned on close of escrow, but it shall be deemed earned even if escrow fails to close if that failure arose from seller's default or lack of good faith.

[*Option 2: Commission on buyer's default*]

If buyer defaults, the commission shall be payable only if and when seller collects damages from buyer, by suit or otherwise, and in an amount not to exceed half the damages recovered after first deducting seller's actual out-of-pocket expenses incurred in connection with the sale (*e.g.,* title, escrow, and inspections and

reports prepared at seller's expense), and any expenses of collection, including but not limited to attorney fees.

[*Option 3: Withdrawal-from-sale clause*]

A commission of _ _ percent of _ _[*dollar amount*]**_ _ shall be payable if seller withdraws the property from sale, encumbers it, leases it, or otherwise renders it unmarketable during the listing period.**

[*Continue*]

[*Add if a printed or form agreement is used; set words below in not less than 10-point bold type to comply with Bus & P C §10147.5*]

Notice: The amount or rate of real estate commissions is not fixed by law. They are set by each broker individually and may be negotiable between the seller and broker.

Comment: The commission amount is usually a percentage of the sales price or, sometimes, a flat fee. When the amount is a percentage, a sliding scale may be used if the percentage decreases (or, rarely, increases) over a certain sales price. Sometimes commission agreements provide for different percentages to be payable, depending on whether the listing broker sells the property or whether a selling broker procures the buyer.

The language in the last paragraph of the form is required by Bus & P C §10147.5. It must be included in any printed or form agreement for the sale of a mobilehome or residential real property containing four or fewer residential units. Section 10147.5 also provides that the amount or rate of compensation shall not be printed in the agreement. See also §2.118.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.80 (5) Form: Buyers Excluded From Agency

§2.80 (5) Form: Buyers Excluded From Agency

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§2.64-2.88.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

2.80-1 Buyers excluded from agency

Broker shall not be entitled to a commission for any sale, lease, exchange, or other transfer to any of the following persons: _ _[*names*]**_ _.**

Comment: A seller who signs a listing agreement with a particular broker may already have brought the property to the attention of one or more prospective buyers or have an obligation to another broker under a safety clause. See form in §2.82; for discussion, see §§2.116-2.117. This provision enables the seller to eliminate any claim by the present broker for a commission on a sale to such a buyer. Under an exclusive right-to-sell listing (see §2.56), this provision is essential to protect the seller in the event of a sale to a buyer with whom the seller or previous broker had negotiated. It is also useful in an open listing (see §2.59) or an exclusive agency listing (see §2.58) to avoid disputes about who procured a particular buyer. Many brokers will not accept a listing containing such an exclusion, or will do so only if the exclusion is limited to a brief period of time.

© The Regents of the University of California

h. Safety Clauses

§2.81 (1) Purpose of Safety Clause

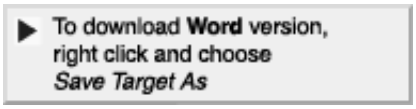
A safety clause or protection clause entitles the broker to the commission if the property is sold within a stated period, after the listing expires, to a buyer identified during the listing term. This type of clause is often contained in exclusive right-to-sell listing agreements. Under the form safety clause in §2.82, the broker must actually have negotiated with the buyer regarding the property. *Simank Realty, Inc. v DeMarco* (1970) 6 CA3d 610, 86 CR 212. The broker need not be the procuring cause of the eventual sale (*Leonard v Fallas* (1959) 51 C2d 649, 335 P2d 665; *Delbon v Brazil* (1955) 134 CA2d 461, 285 P2d 710) unless the agreement calls for that level of involvement (*E.A. Strout W. Realty Agency, Inc. v Lewis* (1967) 255 CA2d 254, 62 CR 918). See §§2.116-2.117 for discussion of safety clauses and the broker's right to recovery.

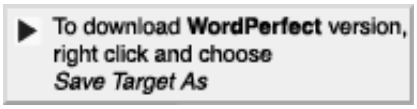
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.82 (2) Form: Sale After Termination of Listing Agreement (Safety or Protection Clause)

§2.82 (2) Form: Sale After Termination of Listing Agreement (Safety or Protection Clause)

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§2.64-2.88.





2.82-1 Sale after termination of listing agreement (safety or protection clause)

If, within _ _[*number*]_ _ days after termination of the listing period or any extension of it, seller agrees to _ _[*sell/lease/transfer/exchange*]_ _ the property _ _[*to/with*]_ _ anyone with whom broker negotiated concerning a possible purchase of the property during the listing period or any extension of it, broker shall be entitled to a commission in the amount and on the terms specified in the listing agreement. Seller shall have no obligation to pay broker any commission under this provision unless, no later than _ _[*number*]_ _ days after expiration of the listing period or any extension of it, broker provides to seller a written list of all parties with whom broker has negotiated for a possible sale.

[*If applicable, add the following option*]

[*Option: Termination on broker's failure to perform*]

This provision shall not apply if seller terminates this agreement because of broker's failure to perform or breach of duty, or if, during the period specified in this provision, a sale of the property is procured by any other licensed real estate broker under a valid listing agreement.

Comment: The protection period is normally 30 to 60 days and requires the broker to notify the owner in writing of parties with whom the broker has negotiated. This language only requires the seller to agree to the sale within the protection period. The more common, but ambiguous language, "if the property is *sold* during the term," should be interpreted the same way. The escrow closing date may determine when the commission is payable, but it should not be relevant to the question of whether it has been earned. See discussion of when property is considered sold in §2.112.

© The Regents of the University of California

i. Broker's Duties

§2.83 (1) Duties Performed; Use of Due Diligence

The duties performed by the broker vary widely. Preprinted listing agreements rarely spell out the broker's duties. Promotion of a particular property may require services beyond those ordinarily performed by the broker selected. If the seller has specific requirements in mind for the broker's performance, the agreement should specify the services to be provided so that the owner can revoke the listing if the broker fails to perform. The seller may, for example, want the agreement to specify marketing services such as advertising (names of newspapers, frequency of appearance of ads, emphasis of special features), signs (size, design, location, wording), photographs, putting the property on the multiple listing service, and restrictions on showing the premises.

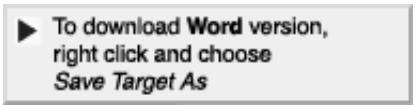
The broker's failure to exercise due diligence in performing its duties may enable the owner to revoke the listing. *Coleman v Mora* (1968) 263 CA2d 137, 69 CR 166; see §2.148 for discussion of the owner's right to revoke. Whether the broker has performed with due diligence is a question of fact that depends on the circumstances of each case (*Whitney Inv. Co. v Westview Dev. Co.* (1969) 273 CA2d 594, 78 CR 302), and there are no precise standards for ascertaining whether the broker's duty has been breached. If the seller has listed the services expected of the broker in as much detail as possible, it will be easier to establish a breach if it occurs. The broker's failure to advertise and offer the property to the public in a nondiscriminatory fashion may breach the duty to exercise due diligence by failing to reach a market that would otherwise be available. *Crowell v Issacs* (1965) 235 CA2d 755, 45 CR 566.

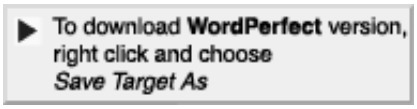
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.84 (2) Form: Broker's Duties

§2.84 (2) Form: Broker's Duties

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§2.64-2.88.





2.84-1 Broker's duties

By accepting this listing, broker agrees to exercise due diligence to procure a buyer and promptly and diligently to do the following: _ _[*describe brokers' duties*]**_ _.**

© The Regents of the University of California

§2.85 j. Arbitration

Any contract to convey real property, or that contemplates a future real property sale, that provides for binding arbitration must set forth the arbitration clause in specific statutory language, and in a particular type size and style. CCP §1298. The arbitration clause also must be separately initialed by the parties. The statutory language informs the parties that, by selecting arbitration, they are waiving certain rights, including the right to a jury trial. These requirements have resulted in litigation over the enforceability of arbitration clauses that did not include the statutory language, or were not in the proper typeface, or were not separately initialed by both parties. Following the United States Supreme Court's decision in *Doctor's Assocs., Inc. v Casarotto* (1996) 517 US 681, 134 L Ed 2d 902, 116 S Ct 1652, §1298 is probably invalid under the Supremacy Clause as an unreasonable restraint on arbitration in contravention of the federal Arbitration Act (9 USC §§1-16), at least in any transaction involving any aspect of interstate commerce (*e.g.,* any transaction where financing is contemplated). *Hedges v Carrigan* (2004) 117 CA4th 578, 11 CR3d 787.

When the statute is enforceable, however, failure to follow its requirements will, at a minimum, invalidate the clause and may invalidate the entire contract. As long as it remains on the books, the careful drafter should continue to observe its technical requirements, even though a straightforward arbitration clause (in normal typeface and without separate initials) should be enforceable. The parties can alter the language of the notice to change, *e.g.,* the method of arbitration or the right to discovery. The parties may also want to specify the number of arbitrators (American Arbitration Association Real Estate Industry Arbitration Rule 19 provides for one arbitrator unless the contract provides for more), the place in which the arbitration will be held, and the time period within which the hearing shall be scheduled.

For an example of an arbitration clause, see paragraph 19B of the California Association of Realtors® Residential Listing Agreement (Exclusive Authorization and Right to Sell) in §2.57. On alternative dispute resolution, see California Real Estate Brokers: Law and Litigation, chap 6 (Cal CEB 2009).

© The Regents of the University of California

k. Execution; Acknowledgment of Receipt

§2.86 (1) Execution

A broker's listing agreement must be executed by the party to be charged. CC §1624(a). The issue of proper execution typically arises in the context of the broker's attempt to recover a commission, and usually the primary question is whether the party executing the listing agreement was actually the owner of the property. Sometimes a principal of the entity that owns the property executes the listing without properly indicating his or her title or authority. At the very least, the person signing the listing will be bound; but the broker should attempt to ensure that the actual seller is bound as well. Sound practice calls for both the seller and the broker to sign the agreement. If a letter agreement is used, the broker should be required to sign and return a copy to the seller. See form 2.88-1. For a discussion of signature requirements in business contracts, see Drafting Business Contracts: Principles, Techniques & Forms §§18.1-18.33 (Cal CEB 1994).

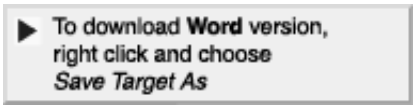
If a rider or an amendment is added to a printed form, both the form and the final page of the separately drafted provisions should be dated and signed and the other pages initialed. See form 2.87-1 for a provision stating the number of pages or provisions of the rider.

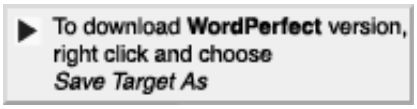
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.87 (2) Form: Printed Form Subordinate to Drafted Provisions

§2.87 (2) Form: Printed Form Subordinate to Drafted Provisions

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§2.64-2.88.





2.87-1 Printed form subordinate to drafted provisions (rider to printed form)

The rider, containing _ _[*pages/provisions*]_ _ numbered _ _ through _ _, executed concurrently with this agreement and appended to it, constitutes an integral part of this agreement and supersedes inconsistent provisions in it.

Comment: Brokers often prefer to use standard listing agreement forms even when they intend to alter them substantially; these altered terms are set out in a specially drafted rider. See §2.62. To make it clear that the printed form is part of a broader agreement, the rider should refer to the printed form.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.88 (3) Form: Acknowledgment of Receipt; Broker's Acceptance

§2.88 (3) Form: Acknowledgment of Receipt; Broker's Acceptance

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§2.64-2.88.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

2.88-1 Acknowledgment of receipt; broker's acceptance

[*Add one of the following alternatives*]

[*Alternative 1: Listing agreement*]

Seller acknowledges receipt of a copy of this listing agreement.

[*Alternative 2: Letter agreement mailed to broker*]

Please sign and return the enclosed copy of this letter as evidence of your agreement to its terms.

Comment: These provisions are designed to protect the broker, who is required to give a copy of the agreement to the person signing it (Bus & P C §10142) and is subject to discipline for failure to do so (Bus & P C §10177). Failure to deliver a copy, however, will not affect the broker's right to a commission under a valid listing agreement. *Summers v Freeman* (1954) 128 CA2d 828, 276 P2d 131.

If the agreement takes the form of a letter to the broker, acknowledgment by the seller is unnecessary and the second alternative should be used to show the broker's assent to the terms of the listing agreement.

© The Regents of the University of California

C. Buyer-Broker Agreements

§2.89 1. General Considerations

It is less common for brokers to earn their commissions from the buyer rather than the seller, although in some markets it is not unusual in certain kinds of commercial transactions for each party to pay its own broker's commission. Even when the broker is employed by the buyer, it is often understood that the buyer's broker must look to the seller to be paid a commission. In many buyer-broker agreements, the principal is a substantial commercial client interested in locating sites for new ventures, and the broker and the principal have worked together over time and have developed a relationship of mutual trust. For these reasons, their agreement is often not reduced to writing until a purchase agreement is executed. In this less formal atmosphere, it is important that the terms of the broker's employment be clearly expressed and understood by both the buyer and the broker. Oral agreements should be put in writing as soon as possible, even if only in the form of a letter, to avoid disputes and misunderstandings.

The buyer may still be liable to pay the broker commission even if the seller releases the buyer from liability for defaulting under the purchase agreement and failing to close escrow. *Schaffter v Creative Capital Leasing Group, LLC* (2008) 166 CA4th 745, 752, 83 CR3d 19 (consequences result when people cancel contracts without valid reason).

The various listing agreement provisions set forth in §§2.64-2.88 can be readily adapted for a buyer-broker agreement, as appropriate, regardless of whether a letter or an employment contract format is used. Provisions that might be desired by the buyer or the broker include employment of the broker and term of the agency (see §2.64), characteristics of the property sought, conditions under which the commission will be earned and by whom it will be paid (see §2.79), a safety clause (see §2.82), and the broker's duties (see §2.84).

In response to the opinion in *Field v Century 21 Klowden-Forness Realty* (1998) 63 CA4th 18, 73 CR2d 784 (buyer-broker has fiduciary duty to client; see §2.124), the California Association of Realtors® revised the buyer-broker agreement. There are now three standard forms: the Buyer Representation Agreement (Nonexclusive/Not for Compensation) (BRNN), the Buyer Representation Agreement—Exclusive (BRE), and the Buyer Representation Agreement—Non-Exclusive (BRNE). See §2.90 for form BRE. In general, the agreements do the following:

- Delineate the scope of the tasks and duties to be performed by buyer and broker;
- Consent to the broker's dual agency; and
- Limit the amount of time a buyer has to bring a legal claim against the broker.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.90 2. Form: Buyer Representation Agreement--Exclusive (CAR Form BRE)

§2.90 2. Form: Buyer Representation Agreement—Exclusive (CAR Form BRE)



CALIFORNIA ASSOCIATION OF REALTORS®

BUYER REPRESENTATION AGREEMENT - EXCLUSIVE

(C.A.R. Form BRE, Revised 4/07)

1. **EXCLUSIVE RIGHT TO REPRESENT:** _____ ("Buyer") grants _____ ("Broker") beginning on (date) _____ and ending at: **(i)** 11:59 P.M. on (date) _____, or **(ii)** completion of a resulting transaction, whichever occurs first ("Representation Period"), the exclusive and irrevocable right, on the terms specified in this Agreement, to represent Buyer in acquiring real property or a manufactured home. Broker agrees to exercise due diligence and reasonable efforts to fulfill the following authorizations and obligations. Broker will perform its obligations under this Agreement through the individual signing for Broker below, who is either Broker individually or an associate-licensee (an individual licensed as a real estate salesperson or broker who works under Broker's real estate license). Buyer agrees that Broker's duties are limited by the terms of this Agreement, including those limitations set forth in paragraphs 6 and 7.
2. **AGENCY RELATIONSHIPS:**
   A. **DISCLOSURE:** If the property described in paragraph 4 includes residential property with one to four dwelling units, Buyer acknowledges receipt of the "Disclosure Regarding Real Estate Agency Relationships" (C.A.R. Form AD) prior to entering into this Agreement.
   B. **BUYER REPRESENTATION:** Broker will represent, as described in this Agreement, Buyer in any resulting transaction.
   C. **(1) POSSIBLE DUAL AGENCY WITH SELLER:** (C)(1) APPLIES UNLESS C(2)(i) or (ii) is checked below.) Depending on the circumstances, it may be necessary or appropriate for Broker to act as an agent for both Buyer and a seller, exchange party, or one or more additional parties ("Seller"). Broker shall, as soon as practicable, disclose to Buyer any election to act as a dual agent representing both Buyer and Seller. If Buyer is shown property listed with Broker, Buyer consents to Broker becoming a dual agent representing both Buyer and Seller with respect to those properties. In event of dual agency, Buyer agrees that: **(a)** Broker, without the prior written consent of Buyer, will not disclose to Seller that the Buyer is willing to pay a price greater than the price offered; **(b)** Broker, without the prior written consent of Seller, will not disclose to Buyer that Seller is willing to sell Property at a price less than the listing price; and **(c)** other than as set forth in (a) and (b) above, a dual agent is obligated to disclose known facts materially affecting the value or desirability of the property to both parties.
   OR (2) SINGLE AGENCY ONLY: (APPLIES ONLY IF (i) or (ii) is checked below.)
   ☐ **(i) Broker's firm lists properties for sale:** Buyer understands that this election will prevent Broker from showing Buyer those properties that are listed with Broker's firm or from representing Buyer in connection with those properties. Buyer's acquisition of a property listed with Broker's firm shall not affect Broker's right to be compensated under paragraph 3. In any resulting transaction in which Seller's property is not listed with Broker's firm, Broker will be the exclusive agent of Buyer and not a dual agent also representing Seller.
   OR ☐ **(ii) Broker's firm DOES NOT list property:** Entire brokerage firm only represents buyers and does not list property. In any resulting transaction, Broker will be the exclusive agent of Buyer and not a dual agent also representing Seller.
   D. **OTHER POTENTIAL BUYERS:** Buyer understands that other potential buyers may, through Broker, consider, make offers on or acquire the same or similar properties as those Buyer is seeking to acquire. Buyer consents to Broker's representation of such other potential buyers before, during and after the Representation Period, or any extension thereof.
   E. **NON CONFIDENTIALITY OF OFFERS:** Buyer is advised that Seller or Listing Agent may disclose the existence, terms, or conditions of Buyer's offer unless all parties and their agent have signed a written confidentiality agreement. Whether any such information is actually disclosed depends on many factors, such as current market conditions, the prevailing practice in the real estate community, the Listing Agent's marketing strategy and the instructions of the Seller.
   F. **CONFIRMATION:** If the Property (as defined below) includes residential property with one to four dwelling units, Broker shall confirm the agency relationship described above, or as modified, in writing, prior to or coincident with Buyer's execution of a Property Contract (as defined below).
3. **COMPENSATION TO BROKER:**
   NOTICE: The amount or rate of real estate commissions is not fixed by law. They are set by each Broker individually and may be negotiable between Buyer and Broker (real estate commissions include all compensation and fees to Broker).
   Buyer agrees to pay to Broker, irrespective of agency relationship(s), as follows:
   A. **AMOUNT OF COMPENSATION: (Check (1), (2) or (3). Check only one.)**
   ☐ **(1)** _____ percent of the acquisition price AND (if checked ☐) $ _____.
   OR ☐ **(2)** $ _____.
   OR ☐ **(3)** Pursuant to the compensation schedule attached as an addendum _____.
   B. **BROKER RIGHT TO COMPENSATION:** Broker shall be entitled to the compensation provided for in paragraph 3A:
   (1) If during the Representation Period, or any extension thereof, Buyer enters into an agreement to acquire property described in paragraph 4, on those terms or any other terms acceptable to Buyer. (Broker shall be entitled to compensation whether any escrow resulting from such agreement closes during or after the expiration of the Representation Period.)
   (2) If, within ___ **calendar days** after expiration of the Representation Period or any extension thereof, Buyer enters into an agreement to acquire property described in paragraph 4, which property Broker introduced to Buyer, or for which Broker acted on Buyer's behalf. The obligation to pay compensation pursuant to this paragraph shall arise only if, prior to or within **3 (or** ☐ _____**) calendar days** after expiration of this Agreement or any extension thereof, Broker gives Buyer a written notice of those properties which Broker introduced to Buyer, or for which Broker acted on Buyer's behalf.

The copyright laws of the United States (Title 17 U.S. Code) forbid the unauthorized reproduction of this form, or any portion thereof, by photocopy machine or any other means, including facsimile or computerized formats. Copyright © 1991-2007, CALIFORNIA ASSOCIATION OF REALTORS®, INC. ALL RIGHTS RESERVED.

Buyer and Broker acknowledge receipt of a copy of this page.

Buyer's Initials (_____)(_____)

Broker's Initials (_____)(_____)

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

C. **PAYMENT OF COMPENSATION:** Compensation is payable:
(1) Upon completion of any resulting transaction, and if an escrow is used, through escrow.
(2) If acquisition is prevented by default of Buyer, upon Buyer's default.
(3) If acquisition is prevented by a party to the transaction other than Buyer, when Buyer collects damages by suit, settlement or otherwise. Compensation shall equal one-half of the damages recovered, not to exceed the compensation provided for in paragraph 3A, after first deducting the unreimbursed expenses of collection, if any.

D. **BUYER OBLIGATION TO PAY COMPENSATION:** Buyer is responsible for payment of compensation provided for in this Agreement. **However, if anyone other than Buyer compensates Broker for services covered by this Agreement, that amount shall be credited toward Buyer's obligation to pay compensation.** If the amount of compensation Broker receives from anyone other than Buyer exceeds Buyer's obligation, the excess amount shall be disclosed to Buyer and if allowed by law paid to Broker, or (if checked) ☐ credited to Buyer, or ☐ other _____.

E. Buyer hereby irrevocably assigns to Broker the compensation provided for in paragraph 3A from Buyer's funds and proceeds in escrow. Buyer agrees to submit to escrow any funds needed to compensate Broker under this Agreement. Broker may submit this Agreement, as instructions to compensate Broker, to any escrow regarding property involving Buyer and a seller or other transferor.

F. **"BUYER"** includes any person or entity, other than Broker, related to Buyer or who in any manner acts on Buyer's behalf to acquire property described in paragraph 4.

G. **(1)** Buyer has not previously entered into a representation agreement with another broker regarding property described in paragraph 4, unless specified as follows (name other broker here): _____
_____
(2) Buyer warrants that Buyer has no obligation to pay compensation to any other broker regarding property described in paragraph 4, unless Buyer acquires the following property(ies): _____.
(3) If Buyer acquires a property specified in G(2) above during the time Buyer is obligated to compensate another broker, Broker is neither: **(i)** entitled to compensation under this Agreement, nor **(ii)** obligated to represent Buyer in such transaction.

4. **PROPERTY TO BE ACQUIRED:** Any purchase, lease or other acquisition of any real property or manufactured home described as follows: _____
_____
Price range: $_____ to $ _____

5. **INTERNET ADVERTISING:** Buyer acknowledges and agrees that: **(i)** properties presented to them may have been marketed through a "virtual tour" on the Internet, permitting potential buyers to view properties over the Internet; **(ii)** neither the service provider nor Broker has control over who will obtain access to the service or what action such persons might take; and **(iii)** Broker has no control over how long the information concerning the properties will be available on the Internet.

6. **BROKER AUTHORIZATIONS AND OBLIGATIONS:**
A. Buyer authorizes Broker to: **(i)** locate and present selected properties to Buyer, present offers authorized by Buyer, and assist Buyer in negotiating for acceptance of such offers; **(ii)** assist Buyer with the financing process, including obtaining loan pre-qualification; **(iii)** upon request, provide Buyer with a list of professionals or vendors who perform the services described in the attached Buyer's Inspection Advisory; **(iv)** order reports, and schedule and attend meetings and appointments with professionals chosen by Buyer; **(v)** provide guidance to help Buyer with the acquisition of property; and **(vi)** obtain a credit report on Buyer.
B. For property transactions of which Broker is aware and not precluded from participating in by Buyer, Broker shall provide and review forms to create a property contract ("Property Contract") for the acquisition of a specific property ("Property"). With respect to such Property, Broker shall: **(i)** if the Property contains residential property with one to four dwelling units, conduct a reasonably competent and diligent on-site visual inspection of the accessible areas of the Property (excluding any common areas), and disclose to Buyer all facts materially affecting the value or desirability of such Property that are revealed by this inspection; **(ii)** deliver or communicate to Buyer any disclosures, materials or information received by, in the personal possession of or personally known to the individual signing for Broker below during the Representation Period; and **(iii)** facilitate the escrow process, including assisting Buyer in negotiating with Seller. Unless otherwise specified in writing, any information provided through Broker in the course of representing Buyer has not been and will not be verified by Broker. Broker's services are performed in compliance with federal, state and local anti-discrimination laws.

7. **SCOPE OF BROKER DUTY:**
A. While Broker will perform the duties described in paragraph 6B, Broker recommends that Buyer select other professionals, as described in the attached Buyer's Inspection Advisory, to investigate the Property through inspections, investigations, tests, surveys, reports, studies and other available information ("Inspections") during the transaction. Buyer agrees that these Inspections, to the extent they exceed the obligations described in paragraph 6B, are not within the scope of Broker's agency duties. Broker informs Buyer that it is in Buyer's best interest to obtain such Inspections.
B. Buyer acknowledges and agrees that Broker: **(i)** does not decide what price Buyer should pay or Seller should accept; **(ii)** does not guarantee the condition of the Property; **(iii)** does not guarantee the performance, adequacy or completeness of inspections, services, products or repairs provided or made by Seller or others; **(iv)** does not have an obligation to conduct an inspection of common areas or offsite areas of the Property; **(v)** shall not be responsible for identifying defects on the Property, in common areas or offsite unless such defects are visually observable by an inspection of reasonably accessible areas of the Property or are known to Broker; **(vi)** shall not be responsible for inspecting public records or permits concerning the title or use of the Property; **(vii)** shall not be responsible for identifying the location of boundary lines or other items affecting title; **(viii)** shall not be responsible for verifying square footage, representations of others or information contained in Investigation reports, Multiple Listing Service, advertisements, flyers or other promotional material; **(ix)** shall not be responsible for providing legal or tax advice regarding any aspect of a transaction entered into by Buyer or Seller; and **(x)** shall not be responsible for providing other advice or information that exceeds the knowledge, education and experience required to perform real estate licensed activity. Buyer agrees to seek legal, tax, insurance, title and other desired assistance from appropriate professionals.

Buyer and Broker acknowledge receipt of a copy of this page.
Buyer's Initials (_____)(_____)
Broker's Initials (_____)(_____)

Copyright © 1991-2007, CALIFORNIA ASSOCIATION OF REALTORS®, INC.

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

C. Broker owes no duty to inspect for common environmental hazards, earthquake weaknesses, or geologic and seismic hazards. If Buyer receives the booklets titled "Environmental Hazards: A Guide for Homeowners, Buyers, Landlords and Tenants," "The Homeowner's Guide to Earthquake Safety," or "The Commercial Property Owner's Guide to Earthquake Safety," the booklets are deemed adequate to inform Buyer regarding the information contained in the booklets and, other than as specified in 6B above, Broker is not required to provide Buyer with additional information about the matters described in the booklets.

8. BUYER OBLIGATIONS:

A. Buyer agrees to timely view and consider properties selected by Broker and to negotiate in good faith to acquire a property. Buyer further agrees to act in good faith toward the completion of any Property Contract entered into in furtherance of this Agreement. Within **5 (or ☐ _____) calendar days** from the execution of this Agreement, Buyer shall provide relevant personal and financial information to Broker to assure Buyer's ability to acquire property described in paragraph 4. If Buyer fails to provide such information, or if Buyer does not qualify financially to acquire property described in paragraph 4, then Broker may cancel this Agreement in writing. Buyer has an affirmative duty to take steps to protect him/herself, including discovery of the legal, practical and technical implications of discovered or disclosed facts, and investigation of information and facts which are known to Buyer or are within the diligent attention and observation of Buyer. Buyer is obligated, and agrees, to read all documents provided to Buyer. Buyer agrees to seek desired assistance from appropriate professionals, selected by Buyer, such as those referenced in the attached Buyer's Inspection Advisory.

B. Buyer shall notify Broker in writing (C.A.R. Form BMI) of any material issue to Buyer, such as, but not limited to, Buyer requests for information on, or concerns regarding, any particular area of interest or importance to Buyer ("Material Issues").

C. **Buyer agrees to: (i) indemnify, defend and hold Broker harmless from all claims, disputes, litigation, judgments, costs and attorney's fees arising from any incorrect information supplied by Buyer, or from any Material Issues that Buyer fails to disclose in writing to Broker; and (ii) pay for reports, inspections and meetings arranged by Broker on Buyer's behalf.**

D. Buyer is advised to read the attached Buyer's Inspection Advisory for a list of items and other concerns that typically warrant Inspections or investigation by Buyer or other professionals.

9. DISPUTE RESOLUTION:

A. **MEDIATION:** Buyer and Broker agree to mediate any dispute or claim arising between them out of this Agreement, or any resulting transaction, before resorting to arbitration or court action, subject to paragraph 9B(2) below. Paragraph 9B(2) below applies whether or not the arbitration provision is initialed. Mediation fees, if any, shall be divided equally among the parties involved. If, for any dispute or claim to which this paragraph applies, any party commences an action without first attempting to resolve the matter through mediation, or refuses to mediate after a request has been made, then that party shall not be entitled to recover attorney's fees, even if they would otherwise be available to that party in any such action. THIS MEDIATION PROVISION APPLIES WHETHER OR NOT THE ARBITRATION PROVISION IS INITIALED.

B. **ARBITRATION OF DISPUTES: (1) Buyer and Broker agree that any dispute or claim in Law or equity arising between them regarding the obligation to pay compensation under this Agreement, which is not settled through mediation, shall be decided by neutral, binding arbitration, including and subject to paragraph 9B(2) below. The arbitrator shall be a retired judge or justice, or an attorney with at least five years of residential real estate law experience, unless the parties mutually agree to a different arbitrator, who shall render an award in accordance with substantive California law. The parties shall have the right to discovery in accordance with California Code of Civil Procedure §1283.05. In all other respects, the arbitration shall be conducted in accordance with Title 9 of Part III, of the California Code of Civil Procedure. Judgment upon the award of the arbitrator(s) may be entered in any court having jurisdiction. Interpretation of this Agreement to arbitrate shall be governed by the Federal Arbitration Act.**

(2) EXCLUSIONS FROM MEDIATION AND ARBITRATION: The following matters are excluded from mediation and arbitration: (i) a judicial or non-judicial foreclosure or other action or proceeding to enforce a deed of trust, mortgage or installment land sale contract as defined in California Civil Code §2985; (ii) an unlawful detainer action; (iii) the filing or enforcement of a mechanic's lien; and (iv) any matter that is within the jurisdiction of a probate, small claims or bankruptcy court. The filing of a court action to enable the recording of a notice of pending action, for order of attachment, receivership, injunction, or other provisional remedies, shall not constitute a waiver of the mediation and arbitration provisions.

"NOTICE: BY INITIALING IN THE SPACE BELOW YOU ARE AGREEING TO HAVE ANY DISPUTE ARISING OUT OF THE MATTERS INCLUDED IN THE 'ARBITRATION OF DISPUTES' PROVISION DECIDED BY NEUTRAL ARBITRATION AS PROVIDED BY CALIFORNIA LAW. YOU ARE GIVING UP ANY RIGHTS YOU MIGHT POSSESS TO HAVE THE DISPUTE LITIGATED IN A COURT OR JURY TRIAL. BY INITIALING IN THE SPACE BELOW YOU ARE GIVING UP YOUR JUDICIAL RIGHTS TO DISCOVERY AND APPEAL, UNLESS THOSE RIGHTS ARE SPECIFICALLY INCLUDED IN THE 'ARBITRATION OF DISPUTES' PROVISION. IF YOU REFUSE TO SUBMIT TO ARBITRATION AFTER AGREEING TO THIS PROVISION, YOU MAY BE COMPELLED TO ARBITRATE UNDER THE AUTHORITY OF THE CALIFORNIA CODE OF CIVIL PROCEDURE. YOUR AGREEMENT TO THIS ARBITRATION PROVISION IS VOLUNTARY."

"WE HAVE READ AND UNDERSTAND THE FOREGOING AND AGREE TO SUBMIT DISPUTES ARISING OUT OF THE MATTERS INCLUDED IN THE 'ARBITRATION OF DISPUTES' PROVISION TO NEUTRAL ARBITRATION."

Buyer's Initials _____/_____ **Broker's Initials** _____/_____

Buyer and Broker acknowledge receipt of a copy of this page.
Buyer's Initials (_____)(_____)
Broker's Initials (_____)(_____)

Copyright © 1991-2007, CALIFORNIA ASSOCIATION OF REALTORS®, INC.

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

Print

Buyer: _____ Date: _____

10. **TIME TO BRING LEGAL ACTION:** Legal action for breach of this Agreement, or any obligation arising therefrom, shall be brought no more than two years from the expiration of the Representation Period or from the date such cause of action may arise, whichever occurs first.
11. **OTHER TERMS AND CONDITIONS:** The following disclosures or addenda are attached:
    A. ☑ Buyer's Inspection Advisory (C.A.R. Form BIA)
    B. ☐ Statewide Buyer and Seller Advisory (C.A.R. Form SBSA)
    C. ☐ _____
    D. ☐ _____
12. **ATTORNEY FEES:** In any action, proceeding or arbitration between Buyer and Broker regarding the obligation to pay compensation under this Agreement, the prevailing Buyer or Broker shall be entitled to reasonable attorney fees and costs, except as provided in paragraph 9A.
13. **ENTIRE AGREEMENT:** All understandings between the parties are incorporated in this Agreement. Its terms are intended by the parties as a final, complete and exclusive expression of their agreement with respect to its subject matter, and may not be contradicted by evidence of any prior agreement or contemporaneous oral agreement. This Agreement may not be extended, amended, modified, altered or changed, except in writing signed by Buyer and Broker. In the event that any provision of this Agreement is held to be ineffective or invalid, the remaining provisions will nevertheless be given full force and effect. This Agreement and any supplement, addendum or modification, including any copy, whether by copier, facsimile, NCR or electronic, may be signed in two or more counterparts, all of which shall constitute one and the same writing.

Buyer acknowledges that Buyer has read, understands, received a copy of and agrees to the terms of this Agreement.

Buyer _____ Date _____

Address _____ City _____ State _____ Zip _____

Telephone _____ Fax _____ E-mail _____

Buyer _____ Date _____

Address _____ City _____ State _____ Zip _____

Telephone _____ Fax _____ E-mail _____

Real Estate Broker (Firm) _____ DRE License # _____

By (Agent) _____ DRE License # _____ Date _____

Address _____ City _____ State _____ Zip _____

Telephone _____ Fax _____ E-mail _____

SAMPLE

THIS FORM HAS BEEN APPROVED BY THE CALIFORNIA ASSOCIATION OF REALTORS® (C.A.R.). NO REPRESENTATION IS MADE AS TO THE LEGAL VALIDITY OR ADEQUACY OF ANY PROVISION IN ANY SPECIFIC TRANSACTION. A REAL ESTATE BROKER IS THE PERSON QUALIFIED TO ADVISE ON REAL ESTATE TRANSACTIONS. IF YOU DESIRE LEGAL OR TAX ADVICE, CONSULT AN APPROPRIATE PROFESSIONAL.
This form is available for use by the entire real estate industry. It is not intended to identify the user as a REALTOR®. REALTOR® is a registered collective membership mark which may be used only by members of the NATIONAL ASSOCIATION OF REALTORS® who subscribe to its Code of Ethics.

Published and Distributed by:
REAL ESTATE BUSINESS SERVICES, INC.
a subsidiary of the California Association of REALTORS®
525 South Virgil Avenue, Los Angeles, California 90020

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

BUYER REPRESENTATION AGREEMENT – EXCLUSIVE (BRE PAGE 4 OF 4)

Comment: This form is reprinted with the permission of the California Association of Realtors®. Endorsement is not

implied.

© The Regents of the University of California

V. BROKER'S COMPENSATION

§2.91 A. Prerequisites to Broker's Right to Commission

To recover the commission, a broker must be licensed as required by Bus & P C §§10130 and 10150 (see §2.2), have a written commission agreement (or listing agreement) with the principal (CC §1624(a)(4); see §§2.43-2.53, 2.96), and have performed in accordance with that agreement (see §§2.99-2.113).

PRACTICE TIP: In most instances the written commission agreement or listing agreement will control the broker's right to a commission; however, it is equally permissible to include the commission provision in the purchase agreement, lease, or in other documents executed by the party obliged to pay the commission. For that reason, the attorney should carefully review all documents in the entire transaction.

On brokers' compensation and claims, see California Real Estate Brokers: Law and Litigation, chap 7 (Cal CEB 2009).

© The Regents of the University of California

§2.92 1. Listing (Seller's) Broker

All types of listing agreements require the listing broker (sometimes referred to as the seller's broker) to demonstrate the procurement of a "ready, willing, and able" buyer to purchase the property on the terms in the listing agreement or other terms accepted by the seller. See §§2.106-2.109. The listing agreement may impose further requirements that must be met before the broker is entitled to the commission. See §§2.110-2.113.

In an open listing (see §2.59), the broker must be the "procuring cause" of the contract between the seller and the buyer in order to earn the commission. In an exclusive agency listing (see §2.58), the broker is entitled to a commission when the property is sold unless the seller was the "procuring cause" of the transaction. In an exclusive right-to-sell listing (see §2.56), the broker earns a commission regardless of who is the procuring cause of the sale. See §§2.99-2.105 for discussion of procuring cause.

© The Regents of the University of California

§2.93 2. Cooperating (Buyer's) Broker

The buyer's broker in the usual transaction, often called a "cooperating broker" or "selling broker," must satisfy requirements in addition to those described in §2.92 to recover compensation.

DRAFTING TIP: Both brokers and attorneys should choose the term of reference carefully when describing the brokers. It is more difficult to follow a provision in a contract or cause of action that refers to "seller's broker" and "selling broker" because the terms are so similar. Although it is important to understand the synonyms, it is recommended that clearly distinguishable terms such as "listing broker" and "cooperating broker," or "seller's broker" and "buyer's broker," be used to distinguish between the two.

The cooperating broker can sue the listing broker for a share of any commission already paid and for a declaratory judgment that the cooperating broker is entitled to share in future payments, but the cooperating broker cannot recover from the listing broker any unpaid portion of the commission. *Iusi v Chase* (1959) 169 CA2d 83, 337 P2d 79. Although there must be an express agreement between the brokers to share the commission, the agreement need not be written. *Iusi v Chase, supra*.

In order to recover from the seller, the cooperating broker must either be a subagent of the listing broker or have a separate written agreement with the seller. Most standard residential purchase and sale agreements and many commercial purchase agreements and leases provide that the seller agrees to pay a commission to both the listing and buyer's brokers. This provision is probably a modification of the original listing agreement and most likely creates an independent contractual relationship between the seller and the buyer's broker for purposes of recovering a commission. See *Olsen v Spomer* (1961) 192 CA2d 99, 13 CR 392, on the listing broker's obligations to the cooperating broker when the seller fails to perform. A cooperating broker may also have an independent right to sue under a third party beneficiary theory, even if the broker is identified only by classification as a cooperating broker. *Colbaugh v Hartline* (1994) 29 CA4th 1516, 35 CR2d 213.

Under a multiple listing arrangement in which the listing broker offers to share compensation but does not appoint the cooperating broker as a subagent, the cooperating broker's right to recover a commission directly from the seller (as opposed to the claim against the listing broker for commission sharing) depends on the commission language, if any, in the listing agreement or purchase and sale agreement. For a further discussion multiple listing services, see §§2.39-2.41.

© The Regents of the University of California

§2.94 3. License Required to Recover Compensation

An agreement to employ an unlicensed person to perform services that require a real estate license is void and unenforceable. *Fellom v Adams* (1969) 274 CA2d 855, 79 CR 633. The licensing requirements are intended to protect the public from incompetent and untrustworthy practitioners (*Schantz v Ellsworth* (1971) 19 CA3d 289, 96 CR 783), and, in furtherance of this policy, an unlicensed agent will not be permitted to recover a commission even if the services were rendered competently (*Davis v Chipman* (1930) 210 C 609, 293 P 40).

To recover the commission, a broker must be licensed at the time the cause of action for compensation accrues (Bus & P C §10136); the broker need not have been licensed when the listing was executed. *Wise v Radis* (1925) 74 CA 765, 242 P 90. Although the literal language of §10136 indicates that the crucial period of time is when the commission is earned, rather than when the services are actually performed, several cases have looked to legislative intent, rather than to the language of the statute, to permit recovery by a broker who was licensed at the time the services were performed, even though the license may have lapsed by the time the payment was due. See *Estate of Lopez* (1992) 8 CA4th 317, 10 CR2d 67 (broker licensed when probate sale was completed—and cause of action accrued—could recover despite lapse of license during time sale was arranged and confirmed); *Cline v Yamaga* (1979) 97 CA3d 239, 158 CR 598 (plaintiff licensed when work performed but not when commission payable); *Page v Principe* (1963) 220 CA2d 151, 33 CR 836 (license revoked after services rendered).

If the broker is unlicensed when the services are performed, and if the commission is paid in the form of a promissory note, the broker cannot recover on the note. *Hoar v Tuley* (1970) 12 CA3d 344, 90 CR 559. If the listing agreement employs the services of two people, one of whom is licensed and one of whom is not, neither person can recover. *Estate of Prieto* (1966) 243 CA2d 79, 52 CR 80. A mere finder or middleman, however, need not be licensed to recover a fee. *Tenzer v Superscope, Inc.* (1985) 39 C3d 18, 216 CR 130; see §2.5.

A broker who agrees to share a commission with an unlicensed individual may not be entitled to receive the commission unless the broker performed services, was ignorant of the activities conducted by the unlicensed person for which a license was required, and was not a joint venturer with the unlicensed person. *Preach v Monter Rainbow* (1993) 12 CA4th 1441, 16 CR2d 320.

A law firm partner who holds a California real estate broker's license may represent a seller who agrees to pay the firm a real estate brokerage commission in lieu of an hourly fee for legal services, but no one in the firm who does not hold a license may perform any acts for which a license is required. 88 Ops Cal Atty Gen 203 (2005).

ETHICAL CONSIDERATIONS: It may be dangerous to blur the line between acting as an attorney in a real estate transaction and also acting as a licensed real estate broker. Aside from the obvious question of whether the attorney's malpractice insurer would cover the attorney or the firm for the attorney's acts as a broker, the duties of an attorney and a broker are separate and distinct and may actually conflict. For instance, a broker representing a seller may have an affirmative duty of disclosure to the buyer but, if simultaneously acting as the seller's attorney, that same broker would have an ethical duty to preserving the seller-client's confidence.

© The Regents of the University of California

§2.95 4. Written Contract Required

Under the Statute of Frauds, an agreement authorizing or employing a broker to purchase or sell real property or to introduce, find, or procure a buyer or seller of real property for compensation is not enforceable unless the agreement is in writing. CC §1624(a)(4). See §§2.44-2.53. A broker may have introduced the buyer and the seller, negotiated the contract between them, and helped to consummate the transaction, yet have no basis to recover a commission without a written agreement.

A memorandum of the agreement to satisfy the Statute of Frauds may be found in one paper or in several documents, including an exchange of letters or telegrams or both. *King v Stanley* (1948) 32 C2d 584, 588, 197 P2d 321. See also *Seck v Foulks* (1972) 25 CA3d 556, 567, 102 CR 170 (it was "of no moment" that "surrounding memorandum" was not signed because it was "clearly relevant" to same subject matter). Once there is a written agreement, the commission amount and payment terms can be modified by an oral agreement (although confirmation in writing is preferable to avoid possible confusion or later dispute). CC §1698(b); *Realty Corp. of Am. v Burton* (1958) 162 CA2d 44, 327 P2d 948.

© The Regents of the University of California

§2.96 5. Broker Must Not Represent Self

A provision in a purchase and sale agreement that allows a commission to be paid to a broker who is also the buyer is unenforceable. Parties representing themselves cannot claim a commission because they have not provided brokerage services, *i.e.*, they have not represented *another*. *Horning v Shilberg* (2005) 130 CA4th 197, 205, 29 CR3d 717 ("Horning did not act as a broker by performing services for another for compensation he expected to receive *as a broker*. Because Horning, as principal, was not entitled to a real estate commission in the first instance, he cannot successfully claim a *lost* commission when escrow did not close"). However, Horning was entitled to receive the difference between the purchase price and the fair market value on the date of the breach. CC §3306. Accordingly, had Horning sought to recover for having received a reduction in the purchase price under §3306, and presented evidence of the fair market value, the result would have been different.

NOTE: Some attorneys, noting that brokers often receive commissions when representing themselves, argue that the *Horning* holding resulted from the fact that the broker was attempting to recover a commission based on a breach of the purchase contract. They suggest that this should be distinguished from the situation in which a broker seeks a commission based on a written commission agreement for a completed transaction in which the broker represented himself or herself. In many cases, however, the issue is moot because the self-representing agent is licensed with a broker who is the one to whom the commission actually is paid (even though the agent ultimately may receive practically all of the commission paid to the broker).

© The Regents of the University of California

§2.97 6. Contract Provisions Govern

When a valid listing agreement exists, the broker's rights and duties arise from it (*Seck v Foulks* (1972) 25 CA3d 556, 102 CR 170), and the broker's right to compensation is found within its terms (*Blank v Borden* (1974) 11 C3d 963, 115 CR 31).

The many reported decisions involving brokers' attempts to collect their commissions underscore the importance of specifying unambiguously in the listing agreement the circumstances under which the commission will be earned. Several issues commonly arise in the brokerage situation, and the courts (and occasionally the legislature) have developed rules for interpreting listing agreements and for determining when the commission is due in the absence of clear and specific provisions in an agreement. Common issues that a practitioner is likely to encounter include whether:

- The broker was the procuring cause in producing the buyer (see §§2.99-2.105);
- The buyer procured is ready, willing, and able (see §§2.106-2.109);
- Payment of the commission depends on some event, such as closing (see §§2.110-2.113);
- The commission is due if the seller withdraws the property from the market (see §2.114); and
- The commission is due if the conveyance occurs after the listing agreement expires (see §§2.115-2.117).

Disputes can be avoided through careful drafting of the listing agreement to specify the conditions that must be satisfied for the commission to be earned. See form 2.79-1 for a sample clause on the broker's right to compensation.

© The Regents of the University of California

§2.98 7. Transactions Other Than Outright Sale

Occasionally, a property owner executes a listing agreement, intending to sell the property, but then enters into a transaction other than a sale. For example, a seller might grant a lease with an option to purchase, enter into a partnership or joint venture, or accept a loan on the property. When these transactions occur, with or without a broker's assistance, the broker's right to compensation may be unclear. Because the contract limits and defines the broker's right to compensation (see §2.97), these other transactions must be analyzed to ascertain whether they come within the events described in the listing agreement or commission agreement as triggering the broker's right to a commission. Even if the restructuring of a transaction is not done solely to avoid paying the commission, the seller must act in good faith and do nothing intentional to discourage, embarrass, or prevent the completion of the purchase. To do so would violate the covenant of good faith and fair dealing. *R.J. Kuhl Corp. v Sullivan* (1993) 13 CA4th 1589, 17 CR2d 425.

Alternative transactions include the following:

- *Option.* When the seller grants an option, the broker is generally not entitled to a commission unless and until the option is exercised (see *Williams v United Cal. Bank* (1963) 223 CA2d 309, 35 CR 788), but the fact that the exercise comes long after expiration of the listing agreement will not defeat the broker's right as long as the option was procured during the listing period (*Anthony v Enzler* (1976) 61 CA3d 872, 132 CR 553). For further discussion of options, see chap 8.
- *Formation of Partnership or Joint Venture.* If the seller elects to form a partnership or a joint venture rather than sell the property, a commission might be earned if the property is conveyed to the partnership or the joint venture and if the listing agreement includes broad language entitling the broker to a commission on "conveyance" of the property. See the California Association of Realtors® Residential Listing Agreement (Exclusive Authorization and Right to Sell) form in §2.57, in which the broker earns a commission if the property is "transferred" or "conveyed." But see *Zelkowitz v Tobin* (1951) 108 CA2d 69, 238 P2d 19, in which a broker who procured a joint venturer was held not to have earned a commission under the listing agreement.
- *Lease or Loan.* A lease or a loan transaction in lieu of a sales transaction probably gives rise to a right to a commission only if the transaction is clearly specified in the agreement between the owner and the broker. But see CC §1086(b), which defines "sell" and "sale" in the context of listing agreements to include leases and exchanges.
- *Partial Sale or Strawman Transaction.* A partial sale of a property is also likely to give rise to a right to a commission. If the transaction is consummated with a sale or transfer to an entity or person closely associated with the original buyer, then the transaction should be closely scrutinized as one created fraudulently or with secret intent to avoid a commission.
- *Real Property Exchange.* A real property exchange using a facilitator and ultimately resulting in a closing of escrow is routinely considered akin to an outright sale. 2 Miller & Starr, California Real Estate §5:54 (3d ed 2000).

© The Regents of the University of California

8. Procuring Cause

§2.99 a. Definition

The issue of whether a particular broker is the procuring cause is relevant in the following circumstances:

- When there is an open listing (see §2.59);
- When there is an exclusive agency listing (see §2.56) and the seller claims to be the procuring cause;
- Under a safety clause (see §2.105);
- When the seller refuses to sell; and
- When the broker has not otherwise earned the commission during the term of the listing agreement.

Whether a broker is the procuring cause of a sale is a question of fact. *Sessions v Pacific Improvement Co.* (1922) 57 CA 1, 206 P 653. "Procuring cause" has been defined as the cause originating a series of events that, without a break in their continuity, result in the contemplated transaction. *Rose v Hunter* (1957) 155 CA2d 319, 317 P2d 1027. The broker must set in motion a chain of events that proximately causes the buyer and the seller to reach an agreement. *Nelson v Mayer* (1954) 122 CA2d 438, 265 P2d 52. If the buyer's broker procures a buyer who is ready, willing, and able to purchase the property on the listing terms, the listing broker is also deemed to be the procuring cause. *Korstad v Hoffman* (1963) 221 CA2d Supp 805, 35 CR 61; *Justy v Erro* (1911) 16 CA 519, 117 P 575.

© The Regents of the University of California

b. Factors to Consider

§2.100 (1) Introduction of Parties

To qualify as the procuring cause, it is not sufficient merely to be the first person to contact the eventual buyer. *Rose v Hunter* (1957) 155 CA2d 319, 317 P2d 1027. Once the broker has introduced buyer and seller, however, the commission cannot be denied on the grounds that the broker was excluded from subsequent negotiations. *Justice v Ackerman* (1960) 183 CA2d 649, 6 CR 921. If the seller and buyer delay execution of the purchase agreement until after the listing period has expired, intending to evade the broker's claim to a commission, each may be liable to the broker for the commission: the seller under the listing agreement and the buyer in tort. *California Auto Court Ass'n v Cohn* (1950) 98 CA2d 145, 219 P2d 511; see §§2.120-2.123. See also *E.A. Strout W. Realty Agency, Inc. v Lewis* (1967) 255 CA2d 254, 62 CR 918 (commission due when broker procured prospective buyers but sellers canceled listing agreement and sold property to brother of buyers for benefit of buyers).

© The Regents of the University of California

§2.101 (2) Showing Property

A broker may not be the procuring cause, even after showing the property to the buyer, if the eventual buyer already knows that the property is available and the broker is not instrumental in closing the sale. *Fitzpatrick v Underwood* (1941) 17 C2d 722, 112 P2d 3. If there is a good faith break in the continuity of the negotiations, preventing the broker from showing that the buyer and seller came to terms as a proximate result of his or her efforts, then the broker is not the procuring cause. *Nelson v Mayer* (1954) 122 CA2d 438, 265 P2d 52. The broker is entitled to the commission, however, if the broker found the prospective buyer or tenant and then is instructed to do nothing further. *Coldwell Banker & Co. v Pepper Tree Office Ctr. Assocs.* (1980) 106 CA3d 272, 278, 165 CR 51, disapproved on other grounds in *Barrett v Bank of America* (1986) 183 CA3d 1362, 229 CR 16.

© The Regents of the University of California

§2.102 (3) Completion of Sale

If the listing agreement states that a commission will be paid only on completion of the sale, *i.e.,* at close of escrow, a broker who procures an acceptable buyer is not entitled to compensation if the transaction fails to close. To earn a commission, the broker must be the procuring cause and the transaction must close. *Cochran v Ellsworth* (1954) 126 CA2d 429, 272 P2d 904; Augustine & Zarrow, California Real Estate Law and Practice §62.30[1] (2007). This analysis also presumes that the seller has not prevented the broker from performing his or her duties. See, *e.g.*, *R.J. Kuhl Corp. v Sullivan* (1993) 13 CA4th 1589, 17 CR2d 425.

The completion of a sale is not necessary, however, unless the listing agreement states that it is a condition to the payment of the commission. See §2.108. Absent such a condition, the broker is considered the procuring cause and is entitled to a commission by bringing to the seller a ready, willing, and able buyer, regardless of whether the sale occurs. *Woodbridge Realty v Plymouth Dev. Corp.* (1955) 130 CA2d 270, 278 P2d 713.

© The Regents of the University of California

§2.103 (4) Type of Listing Agreement

Under an open listing agreement (see §2.59), the broker must prove that he or she alone and no other party, including the seller or any other broker, was the procuring cause of the sale. In an exclusive agency listing (see §2.58), the broker must prove that someone other than the seller was the procuring cause of the sale. If a broker has an exclusive right-to-sell listing (see §2.56), a sale to any party, even if the buyer is procured by the seller or another broker, entitles the broker to compensation. Thus, being the procuring cause is most important for a broker under an open listing or comparable situation in which several brokers may be showing the property and a prospective buyer may be contacted by other brokers. If more than one broker has contributed to completing the sale, the broker seeking the commission must prove that his or her activities were the predominant cause in bringing about the transaction. *Sessions v Pacific Improvement Co.* (1922) 57 CA 1, 206 P 653.

© The Regents of the University of California

§2.104 (5) Cooperating Broker

When a cooperating broker (*i.e.,* the buyer's or tenant's broker) is the procuring cause of the sale, recovery from the listing broker is limited to the terms of the cooperation agreement. If the listing agreement authorizes cooperation with other brokers but does not authorize the division of the commission, the seller is not liable for breach of the listing agreement if the seller paid a full commission to the listing agent. *Colbaugh v Hartline* (1994) 29 CA4th 1516, 35 CR2d 213. Under such circumstances, the only remedy available to the cooperating broker is an action against the listing broker.

© The Regents of the University of California

§2.105 (6) Safety or Protection Clause

Procuring cause may also be an issue if a broker attempts to recover under a safety or protection clause for a transaction that is completed after the listing expires. Listing agreements often provide that the broker is entitled to the commission if a "sale" is made within a specified time after the listing period expires to a buyer with whom the broker had contact during the listing period. See CC §1086(b), (i) for the meaning of "sale" and "sold." See §2.112 for discussion of CC §1086(i). Apparently, §1086(i) would extend the safety clause to entitle the broker to a commission if a binding contract (*i.e.,* a unconditional contract) for a lease or exchange is created during the safety clause period. A safety clause form is set out in §2.82.

The broker typically may recover in this situation if the broker procured the buyer during the listing period. See §§2.115-2.117. If the question of the procuring cause may become an issue, the broker should immediately notify the seller, in writing, of the names of prospective buyers contacted by the broker. When the listing agreement terminates, a prudent broker should provide a written list of prospects to the seller whether or not the listing agreement calls for such action.

NOTE: Sellers should be warned that terminating a listing contract does not necessarily terminate the broker's right to compensation. In *Century 21 Butler Realty, Inc. v Vasquez* (1995) 41 CA4th 888, 49 CR2d 1, the sellers fired the broker. The listing agreement contained a safety clause requiring the broker to provide the seller with a list of prospective buyers. The broker failed to do so. The sellers sold their property after the agreement terminated but within the original time limit of the broker's listing. The court held that the seller owed the commission because the sale had occurred within the listing period, regardless of who was the procuring agent.

© The Regents of the University of California

9. Ready, Willing, and Able Buyer

§2.106 a. Basic Considerations

To earn a commission under any type of listing agreement, the broker must procure a buyer who is "ready, willing, and able" to purchase the property on the terms of the listing agreement. The agreement may require additional conditions to be met before the commission is earned. See §§2.97, 2.110-2.113. An owner who executes an unconditional agreement to sell the property, however, cannot claim, in an effort to avoid paying the broker's commission, that the buyer was not "ready, willing, and able" (*Kopf v Milam* (1963) 60 C2d 600, 35 CR 614), even if it later turns out that the buyer did not have the ability to complete the purchase. See *Cardoza v Moorehouse* (1961) 197 CA2d 76, 17 CR 28.

Satisfaction of the "ready" and "willing" parts of the requirement turns on whether the buyer's offer meets all material terms and conditions of the listing agreement. *Prather v Vasquez* (1958) 162 CA2d 198, 327 P2d 963; see §2.107. If the contract includes conditions (such as an inspection or a financing contingency) that were not in the listing, the buyer is considered "ready" and "willing" only when the conditions are satisfied or waived. *Kopf v Milam, supra*. See also *Born v Koop* (1962) 200 CA2d 519, 19 CR 379 (no right to commission; offer deviated from listing).

An "able" buyer is one who has the legal capacity and financial ability to purchase the property. The broker has the burden of proving the buyer's ability to purchase the property under the listing agreement's terms. *Herring v Fisher* (1952) 110 CA2d 322, 242 P2d 963. Financial ability means that the buyer has sufficient resources available to conclude the sale. *Russell v Ramm* (1927) 200 C 348, 254 P 532. The buyer need not have cash on hand when the offer is made, but must have sufficient property, credit, or other assets to be able to obtain the necessary funds at the prescribed time. *Ramsdell v Krehmke* (1928) 95 CA 195, 272 P 333.

© The Regents of the University of California

§2.107 b. Offer Rejected by Seller

If the seller refuses to sell the property to a ready, willing, and able buyer, the broker is normally still entitled to a commission (*Collins v Vickter Manor, Inc.* (1957) 47 C2d 875, 306 P2d 783; *Martin v Culver Enterprises* (1966) 239 CA2d 925, 49 CR 149), but the broker must be able to prove that the buyer's offer satisfied the terms of the listing agreement, or that the seller waived conditions or frustrated performance by the buyer. If the offer differs materially from the listing, the broker cannot recover a commission. *Dea v Davy* (1957) 150 CA2d 435, 309 P2d 894. This test emphasizes the need for a listing agreement that precisely specifies the important terms of the sale.

Whether an offer differs materially from the listing agreement is a question of fact to be decided in each case. *Rylee v Defini* (1955) 134 CA2d Supp 877, 285 P2d 115. Provisions of the buyer's offer that have been considered sufficiently at variance with the listing terms to justify the seller's rejection include the following:

- A provision allowing prepayment of a seller carry-back note (*Born v Koop* (1962) 200 CA2d 519, 19 CR 379);
- A different method of paying the deposit (*Dea v Davy, supra*);
- A different time for possession (*Adams v Angelich* (1964) 231 CA2d 258, 41 CR 767);
- A liquidated damages provision giving the buyer an inexpensive alternative to performance (*California Land Sec. Co. v Ritchie* (1919) 40 CA 246, 180 P 625); and
- The right to assume an existing loan on the property (*Cottingham v Smith* (1938) 28 CA2d 345, 82 P2d 479).

Whether a deviation will be considered material depends on the parties' intentions and expectations. *Andrews v Waldo* (1928) 205 C 764, 272 P 1052. The facts of each case must be individually evaluated. It is risky to rely on past holdings in determining whether certain terms are material.

© The Regents of the University of California

§2.108 c. Offer Accepted: Sale Not Completed

Unless the listing agreement conditions the broker's commission on consummation of the sale (see §§2.110-2.113), the commission is earned on execution of an unconditional purchase agreement, even if the sale later fails. *Deeble v Stearns* (1947) 82 CA2d 296, 186 P2d 173. If the offer differs materially from the listing (see §2.107) and the seller's acceptance of the offer is conditional, the conditions must be either satisfied or waived before the commission is earned. *Cochran v Ellsworth* (1954) 126 CA2d 429, 272 P2d 904. Similarly, mere execution of a conditional purchase agreement does not entitle the broker to the commission; the conditions must be satisfied or waived. *Kopf v Milam* (1963) 60 C2d 600, 35 CR 614.

If the seller accepts a conforming offer but the transaction fails because of the seller's breach or inability to perform, the broker is entitled to the commission. For example, sellers have been held liable for commissions when they were unable to deliver marketable title (*Coulter v Howard* (1927) 203 C 17, 262 P 751) and when a spouse or a joint tenant refused to join in the transfer (*McAlinden v Nelson* (1953) 121 CA2d 136, 262 P2d 627).

On the broker's right to the deposit if the buyer fails to perform, see §2.119.

PRACTICE TIP: Occasionally, the listing broker is willing to forgo any legal claim or remedy against the seller when the seller has withdrawn from the sale or refused to close. The listing broker's rationale is that it will realize a commission on the ultimate sale and it is better to maintain the relationship than attempt to enforce a right to a commission. The cooperating broker, however, may choose to pursue remedies against the seller and should prepare for that possibility. The broker should request and obtain a copy of the listing agreement, make sure there is a written cooperation agreement, if possible, and make sure there is a separate commission agreement with the seller. Alternatively, the cooperating broker should make sure that the purchase agreement designates the cooperating broker as a third party beneficiary of the purchase agreement for purpose of collecting the commission.

© The Regents of the University of California

§2.109 d. Nonconforming or Conditional Offer Accepted

If the parties execute a purchase agreement on different terms from those in the listing agreement, the seller is presumed to have consented to that variance. *Lathrop v Gauger* (1954) 127 CA2d 754, 274 P2d 730. If the offer was unconditional or the conditions have been satisfied, the broker is no longer required to prove the readiness, willingness, or ability of the buyer in order to earn the commission (*Caine v Briscoe* (1926) 78 CA 660, 248 P 774) unless fraud by the broker or the buyer was used to induce the seller's acceptance (*Wright v Buzzine* (1960) 180 CA2d 426, 4 CR 482). As long as the listing agreement does not state that payment of the commission is conditioned on consummation of the sale (see §§2.110-2.113), a seller who accepts a nonconforming, unconditional offer is liable for the commission. *Jauman v McCusick* (1913) 166 C 517, 137 P 254; *Beazell v Kane* (1954) 127 CA2d 593, 274 P2d 224.

If a conditional purchase agreement is executed, the broker is not entitled to compensation until the conditions have been satisfied or waived. *Kopf v Milam* (1963) 60 C2d 600, 35 CR 614. If a condition benefiting the buyer is waived or satisfied, the seller becomes liable for the commission whether or not the transaction with the buyer is completed. *Wesley N. Taylor Co. v Russell* (1961) 194 CA2d 816, 15 CR 357. If the condition benefits both the buyer and seller, the seller does not become liable for the commission until the condition is either satisfied or waived by both parties. *Yoakum v Tarver* (1967) 256 CA2d 202, 64 CR 7. If the condition is inserted solely for the seller's benefit, the seller will be liable for the commission only after the seller has satisfied or waived the condition. *Kopf v Milam, supra; Devereaux v Harper* (1962) 210 CA2d 519, 26 CR 837.

Once all conditions are satisfied or waived, the broker is entitled to the commission even if the parties later abandon or rescind the purchase and sale agreement (*Weber v Ross* (1958) 159 CA2d 77, 323 P2d 465), unless the listing agreement conditioned payment of the commission on consummation of the transaction (*Cochran v Ellsworth* (1954) 126 CA2d 429, 272 P2d 904; see §§2.110-2.113). The broker is entitled to a commission even if the buyer breaches the agreement to buy. *Lipton v Johansen* (1951) 105 CA2d 363, 370, 233 P2d 648.

© The Regents of the University of California

§2.110 10. Conditional Commission Provision

The broker's right to a commission depends on the terms of the listing agreement (see §2.97), and the parties are free to impose conditions that must be satisfied before the commission is earned. *Blank v Borden* (1974) 11 C3d 963, 115 CR 31.

One of the more common conditions is that the commission will be earned and paid only on close of escrow. The listing agreement must be carefully drafted to state the parties' intention that the event that must occur for the commission to be earned is a condition precedent to earning the commission. *Seck v Foulks* (1972) 25 CA3d 556, 102 CR 170. A mere limitation on the time and manner of payment will not defeat the broker's right to the commission. In *RC Royal Dev't and Realty Corp. v Standard Pac. Corp.* (Sept. 29, 2009, B206894) 2009 Cal App Lexis 1606, a broker and a buyer entered into an agency agreement which stated that a commission was due if the property was "purchased." The agency agreement defined "purchase" to mean that the buyer acquired a direct or indirect beneficial interest in the property. The court noting that the buyer, by entering into a buy-sell agreement, had acquired conditional, equitable title which was a beneficial interest and therefore, owed the commission even though escrow never closed. The reference in the agency agreement that the commission would be paid at closing merely designated the timing of the payment and was not a condition to payment. See also *Miller v Lerdo Land Co.* (1921) 52 CA 662, 199 P 1073.

Even under a conditional commission provision, sellers remain liable for payment of the commission if they unreasonably prevent the occurrence of the condition on which payment of the commission depends (*Collins v Vickter Manor, Inc.* (1957) 47 C2d 875, 306 P2d 783) or act in bad faith in failing to complete the transaction (*Stromer v Browning* (1966) 65 C2d 421, 55 CR 18). The purpose of the condition is to protect a seller from the buyer's failure to perform. The commission cannot be recovered if the buyer refuses to perform or satisfy the condition. *Cochran v Ellsworth* (1954) 126 CA2d 429, 272 P2d 904. Furthermore, the broker cannot compel the seller to sue the buyer for breach as a means of recovering the commission. *Dunne v Colomb* (1923) 192 C 740, 221 P 912.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.111 a. Examples of Conditions

§2.111 a. Examples of Conditions

Listing agreement conditions are primarily intended to protect the seller from having to pay a commission if no sales proceeds are realized. Examples of conditions that have been used successfully include:

- Payment of commission on completion of the transaction, *e.g.,* when the purchase price is paid and title is transferred (*Cochran v Ellsworth* (1954) 126 CA2d 429, 272 P2d 904);
- Payment of commission out of funds received from escrow (*Dale v Raines* (1953) 115 CA2d 309, 252 P2d 22); and
- Payment of commission out of funds received from the buyer (*Cannon v Selmser* (1927) 85 CA 783, 260 P 332).

© The Regents of the University of California

b. Provisions in Standard Forms

§2.112 (1) Residential Exclusive Authorization and Right to Sell

The safety clause in the Residential Listing Agreement (Exclusive Authorization and Right to Sell) form (see §2.57), published by the California Association of Realtors® (CAR), states that the commission is due when the seller sells, conveys, leases, or otherwise transfers the property. A property is considered sold "when a legally binding commitment to sell the property comes into existence." CC §1086(i). Thus, absent the provisions for method and time of payment in these agreements, the commission would be earned under §1086(i) when the seller's obligation becomes binding, regardless of whether the transaction is a sale, a lease, or an exchange.

Although CC §1086(i) seems to provide that a property is sold when the seller is bound to sell, regardless of conditions precedent to the buyer's obligation to buy, this interpretation would lead a broker to have potentially earned a commission even if the buyer's conditions are never satisfied. Such a result is not what the legislature intended in enacting §1086, and the better interpretation is that a property is "sold" when all conditions are satisfied and the obligations of both buyer and seller are binding. There are no reported cases addressing this perceived flaw in §1086(i). Case law has defined a "sale" to mean the making of an executory contract by which the property is to be sold. *Leonard v Fallas* (1959) 51 C2d 649, 652, 335 P2d 665.

© The Regents of the University of California

§2.113 (2) Real Estate Residential Purchase Agreement and Receipt for Deposit

The California Association of Realtors® Residential Purchase Agreement and Joint Escrow Instructions (see §6.24) provides that the commission is to be paid on close of escrow or, if escrow does not close, pursuant to a separate written agreement. It is possible that this language conditions the earning of a commission on the occurrence of one of the enumerated events rather than on the property merely being sold within the meaning of CC §1086(i). There are no reported cases, however, deciding whether the CAR residential purchase agreement creates additional conditions to the earning of the commission or whether the contract merely specifies the time and method for payment of the commission. See *Steve Schmidt & Co. v Berry* (1986) 183 CA3d 1299, 228 CR 689; *Austin v Richards* (1956) 146 CA2d 436, 304 P2d 132. Usually, the seller will argue that a commission need not be paid unless the transaction closed.

© The Regents of the University of California

§2.114 B. Broker's Rights Under Withdrawal-From-Sale Clause

Some listing agreements provide that the broker is entitled to a commission if the seller withdraws the property from sale or otherwise renders it unmarketable during the listing period. See, *e.g.,* the California Association of Realtors® Residential Listing Agreement (Exclusive Authorization and Right to Sell) form in §2.57. Somewhat reluctantly, the California courts have enforced withdrawal-from-sale clauses. *Alderson v Houston* (1908) 154 C 1, 96 P 884; *Baumgartner v Meek* (1954) 126 CA2d 505, 272 P2d 552. In *Ertell v Lloyd's Food Prods.* (1953) 115 CA2d 615, 252 P2d 683, the validity of such a provision was recognized, but the court held that the seller's act of leasing a portion of the property enhanced the property's value for sale and thus did not reduce its marketability. In *Blank v Borden* (1974) 11 C3d 963, 115 CR 31, the supreme court concluded that withdrawal-from-sale clauses are enforceable on the rationale that they constitute a true option for the seller rather than a penalty for forfeiture. If the withdrawal-from-sale clause is enforced, the broker recovers the entire commission, even when the seller decides not to sell and has, in fact, realized nothing. Recovery is not limited to amounts actually spent by the broker. *Blank v Borden, supra*.

A seller's repudiation of a listing agreement may also entitle the broker to sue for the commission without first producing a ready, willing, and able buyer, on a theory of anticipatory breach of contract. *Daum v Superior Court* (1964) 228 CA2d 283, 39 CR 443. As a practical matter, a broker may have difficulty recovering a commission if the sale has not closed, unless the broker can demonstrate both substantial effort to market and/or procure a buyer and bad faith conduct on the part of the seller.

© The Regents of the University of California

C. Sale After Listing Period

§2.115 1. When Broker Can Recover Commission

To earn a commission, a broker must perform the services contracted for within the period of time in the listing agreement or any extensions granted by the seller. *Lawrence Block Co. v Scholer* (1958) 166 CA2d 608, 333 P2d 396; *Ridgway v Chase* (1954) 122 CA2d 840, 265 P2d 603. Typically, this means that the property must be sold within the term of the listing. Because CC §1086(i) defines "sold" as the creation of a binding legal commitment to sell (see §§2.110-2.113), the execution of an unconditional, binding contract during the term of the listing will entitle the broker to a commission even if the close of escrow occurs after the listing has expired (assuming that the listing agreement entitled the broker to a commission when the property was sold). This result is also achieved contractually because most listing agreements contain a "safety clause." See §§2.116-2.117.

A broker who procures a buyer after the listing agreement expires is generally prohibited by the Statute of Frauds from recovering a commission. *Augustine v Trucco* (1954) 124 CA2d 229, 268 P2d 780. This rule is subject to two judicially created exceptions that arise when the broker procures a buyer who is ready, willing, and able to meet the terms of the listing but a binding purchase agreement is not executed during the listing period.

Under the first exception, the termination date in a written contract of employment will be considered extended, or the time limitation waived, and the broker will be entitled to a commission if: (1) the owner urged and encouraged the broker to continue efforts to find a buyer for the property after the expiration date in the employment agreement; (2) the broker did so continue with the knowledge, approval, and encouragement of the owner; and (3) the owner sells the property to a buyer who is produced as a result of the broker's efforts. *Kraemer v Smith* (1960) 179 CA2d 52, 3 CR 471 (rejecting seller's argument that the original exclusive agency contract had terminated and any authorization in existence between the parties after that date was oral and unenforceable). If the broker subsequently procures an acceptable buyer, the requirement of performance within the listing period is considered waived, and the Statute of Frauds is not a bar to such a waiver. *Lewis v Foppiano* (1957) 150 CA2d 752, 310 P2d 658.

Under the second exception, if the broker procures a buyer who meets the terms of the listing agreement during the listing period, but the purchase agreement is not executed until after the period has expired, the broker may recover the commission. *De La Questa v Armstrong Holdings Co.* (1920) 48 CA 487, 192 P 135. Further, under some safety clauses (see §§2.116-2.117), the broker need not prove that he or she is the ultimate procuring cause of the eventual transaction. See also *Torelli v J.P. Enters*. (1997) 52 CA4th 1250, 61 CR2d 76 (promise to pay does not die with expiration of counter offer; see further discussion of *Torelli* in §2.52).

© The Regents of the University of California

§2.116 2. Activity Required to Recover Under Safety Clause

The extent of activity required for the broker to recover under a safety clause varies but is generally strictly construed under the terms of the listing agreement. Some listing agreements require only that the buyer have been "introduced" to the property by the broker. *Korstad v Hoffman* (1963) 221 CA2d Supp 805, 35 CR 61. Others require the broker to have "negotiated" with the buyer. *Delbon v Brazil* (1955) 134 CA2d 461, 285 P2d 710. Still others require that the buyer be "procured" by the broker. *E.A. Strout W. Realty Agency, Inc. v Lewis* (1967) 255 CA2d 254, 62 CR 918. See §§2.99-2.105 for discussion of procuring cause. Safety clauses often also require the broker to "register" or give the seller written notice of the names of potential buyers that the broker contacted during the listing period. Many safety clauses require registration within a specified period of time.

The performance specified has a significant bearing on the broker's right to the commission. If the safety clause requires only introduction or negotiation by the broker, then the broker can recover the commission without proving that he or she was the procuring cause of the eventual sale. *Leonard v Fallas* (1959) 51 C2d 649, 335 P2d 665; *Delbon v Brazil, supra*. Courts have, however, generally required that the broker demonstrate some activity in connection with the ultimate sale beyond simply having contacted the prospective buyer. *Hobson v Hunt* (1922) 59 CA 679, 211 P 242. In *Simank Realty, Inc. v DeMarco* (1970) 6 CA3d 610, 86 CR 212, a broker with an exclusive right-to-sell listing containing a safety clause was denied a commission when the owner sold the property 1 day after the listing expired, because the broker did not show the buyer the property or negotiate with him, although the broker's sign had "flagged" the buyer's interest in the property. The typical exclusive listing agreement, however, also contains a provision requiring the seller to refer all prospects to the listing broker; so any quick sale on termination of the listing will be suspect.

If the safety clause provides that the commission will be earned only if the broker actually procures a sale, it will be enforced according to its terms and the broker must prove that he or she was the procuring cause. *E.A. Strout W. Realty Agency, Inc. v Lewis, supra*.

© The Regents of the University of California

§2.117 3. Danger of Liability for Two Commissions

If a safety clause does not require the broker to be the procuring cause in order to recover the commission, the seller could be liable for two commissions on the same sale. See, *e.g., Delbon v Brazil* (1955) 134 CA2d 461, 285 P2d 710, in which the listing broker recovered a commission even though a different broker was actually the procuring cause of the sale. A similar result might occur when there is a second listing that is an exclusive listing with no specified exceptions.

PRACTICE TIP: One way for the seller to avoid this problem is to provide in the second listing agreement that no commission will be earned for sales to prospective buyers named in the notification given by the first broker. A form for this purpose is set out in §2.80.

Previous versions of the CAR exclusive authorization and right-to-sell form avoided this problem by waiving the safety clause for a sale that occurred during the protection period if a valid listing agreement had been entered into with another broker. The 2006 version of that form has deleted the relisting exception; therefore, the first broker is entitled to compensation if the "protected" buyer purchases the property during the protection period, even if the seller lists the property for sale with another real estate broker. See §2.57. For more information about the CAR exclusive listing form, see Chin, *Significant Developments in Residential Sales*, 21 CEB Real Prop L Rep 72, 77 (Apr. 1998). Many multiple listing services (see §§2.39-2.41) provide that, when there is a second listing, either the first broker earns no commission or the commission will be divided.

© The Regents of the University of California

§2.118 D. Amount of Commission

The amount of the commission is governed by the listing agreement negotiated by the parties. See §2.97. If the listing agreement does not fix the amount, a reasonable commission will be allowed. *Beazell v Schrader* (1963) 59 C2d 577, 30 CR 534.

PRACTICE TIP: In analyzing the proper amount of a commission, attorneys should carefully inspect and compare references to commissions in the purchase agreement or lease and obtain all written communications between the parties. To the extent the terms of a purchase agreement or lease differ materially from those in the listing agreement, they may be construed as modifying the listing agreement. Similarly, a series of letters or e-mails that discuss the commission may be construed as a modification to the listing agreement. See *King v Stanley* (1948) 32 C2d 584, 588, 197 P2d 321.

Commissions vary according to the broker, the region, the type of property, and the relative bargaining positions of the parties to the agreement. Brokers commonly charge a percentage of the selling price, although occasionally a broker will accept a flat fee. In large transactions, sellers may prefer a schedule of declining percentages. The commission due under a percentage arrangement is generally computed on the total sale price regardless of the dollar amount of the encumbrances on the property. In installment sales (see chap 9), sellers usually either try to receive enough in the first installment to cover the commission or provide in the listing agreement that the commission will be paid in installments.

Brokers' attempts to set the amount of their commissions have been subject to several legal constraints. Agreements among brokers to fix commission rates violate federal and state antitrust laws. In *McLain v Real Estate Bd.* (1980) 444 US 232, 62 L Ed 2d 441, 100 S Ct 502, the Supreme Court held in a private action that the effect of the defendant's brokerage activities on interstate commerce was sufficient to establish jurisdiction under the Sherman Antitrust Act (15 USC §§1-7). Local Boards of Realtors® have also been held subject to the Cartwright Act (Bus & P C §§16700-16770). *Marin County Bd. of Realtors v Palsson* (1976) 16 C3d 920, 130 CR 1; *Glendale Bd. of Realtors v Hounsell* (1977) 72 CA3d 210, 139 CR 830. See also §2.41.

California statutes and regulations further restrict broker activity in establishing commission rates. For example, Bus & P C §10147.5 requires the following:

- Printed listing agreement forms must state that the commission is not fixed by law and may be negotiated between the seller and the broker; and
- The commission amount shall not be printed in any listing agreement.

Regulations of the Real Estate Commissioner subject the broker to discipline for stating or implying to the seller that the broker is precluded by law, regulation, or the rules of an organization from charging less than the commission the broker has quoted. Bus & P C §§10167, 10177.

In *Bartley v California Ass'n of Realtors* (1980) 115 CA3d 930, 173 CR 284, allegations that a widely used California Association of Realtors® broker's contract for employment of an independent-contractor salesperson provided for a fixed commission rate were held insufficient to support a cause of action for an antitrust civil conspiracy.

© The Regents of the University of California

§2.119 E. Buyer's Breach: Broker's Right to Deposit or Damages

Some purchase agreements limit the broker's commission to no more than one-half of any damages the seller is able to recover, minus expenses, in the event of a breach by the buyer. This provision in an executed purchase agreement, to the extent it is signed, ratified, or accepted by the broker, supersedes the listing agreement and limits the commission to one-half of any amounts actually recovered by the seller. If no funds are retained or recovered by the seller, and presuming that the broker has signed, ratified, or accepted the purchase agreement as a bona fide agreement, the broker is entitled to nothing. *Chapman v Gilmore* (1963) 221 CA2d 506, 34 CR 515. Moreover, the seller has no obligation either to retain the deposit (*Huttlinger v Far W. Enters.* (1955) 131 CA2d 808, 281 P2d 554) or to bring an action against the buyer for damages (*Lipton v Johansen* (1951) 105 CA2d 363, 233 P2d 648). An executed purchase agreement, however, constitutes compliance with the Statute of Frauds and entitles the broker to one-half of the deposit or damages, despite the absence of a listing agreement. *Beazell v Kane* (1954) 127 CA2d 593, 274 P2d 224.

NOTE: A cooperating broker is entitled to the full commission from a buyer when the buyer has refused to complete the transaction without cause, unrestricted by the contract provision. See *Chan v Tsang* (1991) 1 CA4th 1578, 3 CR2d 14.

The obvious source of recovery for both the seller and the broker in the event of the buyer's breach is the deposit. The seller's right to retain the deposit as liquidated damages is strictly circumscribed by statute. CC §§1671-1681. A liquidated damages provision in an agreement to purchase real property must be printed in at least 10-point bold type or in contrasting red print in at least 8-point bold type, and must be separately initialed by both buyer and seller. CC §1677. In a sale of residential property (defined as a dwelling containing no more than four units in which the buyer intends to reside), the provision is valid only if the deposit is actually paid and does not exceed 3 percent of the purchase price. CC §1675. See §§4.142, 6.10-6.13 on liquidated damages.

If the seller retains the deposit under a purchase agreement containing a valid liquidated damages provision and a provision entitling the broker to one-half of any funds recovered by the seller, the broker's commission will be one-half of the deposit. The amount the broker is entitled to recover in this situation may be significantly less than the amount of the commission. If more than one payment is to constitute liquidated damages, a separate liquidated damages clause meeting the requirements of CC §§1675 and 1677 must be executed for each payment. CC §1678.

© The Regents of the University of California

F. Recovery of Commission From Buyer

§2.120 1. Implied Covenant to Complete Purchase

Under both listing and purchase agreements, the seller is usually required to pay whatever commissions are due. If the broker is retained by a buyer, however, and the broker located property that the owner agrees to sell at the price offered, the law implies a promise by the buyer to complete the transaction and treat the broker as a third party beneficiary of the purchase agreement between the buyer and the seller. A buyer who then breaches the purchase agreement is liable to the broker for the commission. *Chan v Tsang* (1991) 1 CA4th 1578, 3 CR2d 14; *Donnellan v Rocks* (1972) 22 CA3d 925, 99 CR 692. Moreover, the broker is entitled to the commission he or she would have earned if the buyer had performed. *Chan,* 1 CA4th at 1583.

This rule applies only when the broker and the buyer stand in the relationship of agent and principal. When the broker is employed by the seller, courts have not permitted recovery of the commission from the buyer on the implied promise rationale. *Hunter v Vernon* (1948) 85 CA2d 525, 193 P2d 139. Under such circumstances, however, the broker may have a claim against the seller, and correspondingly, the seller may have a right of indemnity against the buyer.

© The Regents of the University of California

§2.121 2. Interference With Prospective Economic Advantage

A broker may be able to use the cause of action for tortious interference with prospective economic advantage to recover the commission from the buyer when the seller has a technical defense such as failure to comply with the Statute of Frauds. *Buckaloo v Johnson* (1975) 14 C3d 815, 122 CR 745, disapproved on other grounds in *Della Penna v Toyota Motor Sales, U.S.A.* (1995) 11 C4th 376, 45 CR2d 436 (see discussion in §2.122). See also *Keely v Price* (1972) 27 CA3d 209, 103 CR 531 (action for interference with advantageous economic relationship based on defendant's alleged inducement of other buyers not to pay plaintiff's commission was not barred by fact that agreement was oral); *Zimmerman v Bank of America* (1961) 191 CA2d 55, 12 CR 319 (tort of interference with advantageous relationship or contract did not depend on nature or enforceability of contract itself). These cases arise when a buyer, who is originally contacted by the broker, approaches the seller directly and induces the seller to close the sale without involving the broker, lowering the price by the commission that would otherwise be paid. Occasionally, buyers have purchased property through other parties in an attempt to conceal this conduct. *Golden v Anderson* (1967) 256 CA2d 714, 64 CR 404.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.122 a. Elements of Cause of Action

§2.122 a. Elements of Cause of Action

The broker need not plead and prove the existence of a contract in order to recover under a tortious interference theory, because it is interference with an economic relationship, not a contract, that is the gravamen of the action. In *Buckaloo v Johnson* (1975) 14 C3d 815, 122 CR 745, disapproved on other grounds in *Della Penna v Toyota Motor Sales, U.S.A.* (1995) 11 C4th 376, 45 CR2d 436, the supreme court identified the elements of the cause of action:

- An economic relationship between broker and seller having the probability of future economic benefit to the broker;
- The buyer's knowledge of the existence of the relationship;
- The buyer's intentional acts designed to disrupt the relationship;
- Actual disruption of the relationship; and
- Damages proximately caused by the buyer's actions.

Since *Buckaloo,* the supreme court has clarified the nature of the acts and intent that must be shown to satisfy the third element of the tort. With respect to conduct, the plaintiff must plead that the defendant engaged in an independently wrongful act. *Korea Supply Co. v Lockheed Martin Corp.* (2003) 29 C4th 1134, 1164, 131 CR2d 29; *Della Penna v Toyota Motor Sales, U.S.A.* (1995) 11 C4th 376, 45 CR2d 436. For this purpose, an act is independently wrongful "if it is… proscribed by some constitutional, statutory, regulatory, common law, or other determinable legal standard." *Korea Supply Co.,* 29 C4th at 1159. "It is not enough that the act was a product of an improper, but lawful motive; it must be wrongful by some legal measure." 29 C4th at 1159 n11. With respect to intent, the plaintiff need not plead that the defendant had a specific intent or design to interfere with the plaintiff's prospective advantage. Rather, it is enough if the plaintiff pleads that the defendant acted with the "knowledge that interference was certain or substantially certain to occur as a result of its action." 29 C4th at 1164.

© The Regents of the University of California

§2.123 b. Problems of Proof

Although the leading cases, which all arose on demurrers, hold that a cause of action for tortious interference can be stated, the problems of proof remain substantial. Under the test announced in *Buckaloo v Johnson* (1975) 14 C3d 815, 122 CR 745, disapproved on other grounds in *Della Penna v Toyota Motor Sales, U.S.A.* (1995) 11 C4th 376, 45 CR2d 436 (see discussion in §2.122), the broker must prove the following:

- The economic relationship was one that included the probability of future economic benefit;
- The buyer knew of the relationship; and
- The buyer proposed to the seller that the parties deal directly with each other to obtain a lower price.

A broker's cause of action against the buyer for tortious interference with prospective economic advantage will not lie when the prospective economic advantage itself is fraudulent, as in the case of a secret commission payable by the seller and not disclosed to the buyer. *Renaissance Realty, Inc. v Soriano* (1981) 120 CA3d Supp 13, 174 CR 837.

For an example of the broker's use of a cause of action for interference with prospective economic advantage to sue a buyer for a commission when no written commission agreement existed, see *Deeter v Angus* (1986) 179 CA3d 241, 224 CR 801 (allegation that buyer orally agreed to pay broker's commission if seller would reduce purchase price).

© The Regents of the University of California

VI. BROKER'S FIDUCIARY DUTIES TO CLIENT

§2.124 A. Standard of Care

The legal standards imposed on real estate brokers in relationships with their clients are based on the common law of agency; thus, a real estate broker owes fiduciary obligations to its principal. *Batson v Strehlow* (1968) 68 C2d 662, 68 CR 589; *Ward v Taggart* (1959) 51 C2d 736, 336 P2d 534. The broker's duties are similar to those owed by a trustee to the beneficiary of a trust (Prob C §§16000-16015). The broker owes a duty of utmost care, integrity, honesty, and loyalty in dealings with the principal, in addition to the more general duties (*e.g.,* good faith and fair dealing, diligent exercise of skill and care) owed to both parties to the transaction.

For discussion of a real estate broker's fiduciary duty, see *Jorgensen v Beach 'N' Bay Realty, Inc.* (1981) 125 CA3d 155, 177 CR 882. For a further discussion of broker as agent, see §§2.36-2.42. On brokers' duties and liabilities to principals, see California Real Estate Brokers: Law and Litigation, chaps 3-4 (Cal CEB 2009).

© The Regents of the University of California

§2.125 1. Duty Arises When Agency Created

The broker's fiduciary duties generally arise at the creation of the agency relationship, which may precede the execution of a formal employment contract or may exist in the absence of a written agreement (see §2.27). *Realty Projects, Inc. v Smith* (1973) 32 CA3d 204, 108 CR 71 (mortgage loan broker's duty of fair and honest dealing arises when borrower is only prospective and before any loan documents have been executed). The broker does not, however, owe any fiduciary duty to the client in connection with the negotiation of the terms of the broker's employment.

Although a written agreement is required for a broker to recover a commission (see §2.95), the agency relationship can be created with little or no formality, and is not subject to the Statute of Frauds. The broker, however, does have the duty to preserve the confidentiality of information obtained from the seller even before execution of the listing agreement. *Beeler v West Am. Fin. Co.* (1962) 201 CA2d 702, 20 CR 190.

© The Regents of the University of California

§2.126 2. Duty May Survive Closing

Although selling the property generally terminates the agency relationship, the broker's fiduciary duties include certain post-closing obligations related to the sale. *Menzel v Salka* (1960) 179 CA2d 612, 4 CR 78. The broker's fiduciary duty requires that, even after the expiration of the agency, the broker not disclose or take advantage of confidential information acquired from the client, although the case of *Stephens, Partain & Cunningham v Hollis* (1987) 196 CA3d 948, 242 CR 251, seems to suggest that after the agency relationship has terminated, the broker can take a position that conflicts with that of its former principal (loan broker permitted to act as foreclosing trustee on deed of trust given when broker initially arranged for loan). 3 Witkin, Summary of California Law, *Agency and Employment* §64 (10th ed 2005); Restatement (Second) of Agency §396 (1958).

© The Regents of the University of California

§2.127 B. Duty to Disclose

The broker must fully and completely disclose to the client all facts material to the pending transaction. CC §2020. See *Zikratch v Stillwell* (1961) 196 CA2d 535, 16 CR 660. The broker's duty to the client to disclose material facts is a fiduciary duty and arises on the creation of the principal-broker relationship, *i.e.*, even before the purchase contact is created. *Exxess Elecronixx v Heger Realty Corp.* (1998) 64 CA4th 698, 75 CR2d 376. Material facts include any that might influence the price the client is willing to pay or receive, including the client's willingness to sell or buy. *Rattray v Scudder* (1946) 28 C2d 214, 169 P2d 371; *Fisher v Losey* (1947) 78 CA2d 121, 177 P2d 334. Some of the specific matters that must be disclosed are discussed in §§2.129-2.135.

A broker's duty of disclosure is limited to material facts and once the essential facts are disclosed, a broker is not under a duty to provide details that would elaborate on the disclosed facts. See *Pagano v Krohn* (1997) 60 CA4th, 1, 8; cited in *Calemine v Samuelson* (2009) 171 CA4th 153, 161 (seller's disclosure of water intrusion adequate, but triable issue of fact existed concerning whether seller should have disclosed existence of prior constructive defect litigation as a matter affecting value and desirability of property).

A buyer's broker has no duty to verify the accuracy of the seller's disclosures or those of the seller's broker. It is incumbent on potential purchasers, therefore, to investigate and make their own informed decision. In presenting the client with information obtained from the seller or other third parties, however, the broker should inform the client of the source of the information and the fact that it has not been verified, if circumstances otherwise might lead the client to believe that the broker had done so. Liability may arise if the client reasonably believes that the information was obtained from the broker's own investigation. See *Salahutdin v Valley of Cal., Inc*. (1994) 24 CA4th 555, 29 CR2d 463.

The broker has no heightened duty to disclose or investigate merely because the property is located in a planned unit development. See *Padgett v Phariss* (1997) 54 CA4th 1270, 63 CR2d 373, in which the court held that the brokers had neither a statutory nor a common law duty to discover and disclose matters regarding a pending construction defect lawsuit that the sellers failed to disclose, when the broker's visual inspection of the property provided no reason to conduct a further investigation. See also *Assilzadeh v California Fed. Bank* (2000) 82 CA4th 399, 98 CR2d 176.

The broker's duty of disclosure does not include a duty to verify the truth or explain the legal or practical implications of disclosed facts. See *Pagano v Krohn* (1997) 60 CA4th 1, 70 CR2d 1. For a similar decision holding that a listing agent does not have such a duty, see *Sweat v Hollister* (1995) 37 CA4th 603, 43 CR2d 399, overruled on other grounds in *Santisas v Goodin* (1998) 17 C4th 599, 609, 71 CR2d 830 (discussion of legal ramifications of disclosed facts not required).

© The Regents of the University of California

§2.128 1. Conflicts of Interest

Consistent with the law of agency, the broker's fiduciary duty to its client includes a duty of utmost loyalty, which requires the broker to avoid any conflict of interest and to put the client's interests ahead of those of the broker itself. *Field v Century 21 Klowden-Forness Realty* (1998) 63 CA4th 18, 25, 73 CR2d 784. However, there are exceptions to this rule when the conflict of interest is fully disclosed and the client's informed consent is obtained. See discussion of dual agency in §2.129.

© The Regents of the University of California

§2.129 a. Dual Agency

A broker may not act as an agent for more than one party to a transaction without full disclosure to all parties and their consent. Bus & P C §10176(d). A dual agency may exist, even though the buyer and seller are represented by different agents in different offices, if the agents are licensed under the same broker. CC §2079.13(d).

Dual agency should be disclosed at the earliest practical time, and the clients' consent generally should be obtained in writing. In a residential transaction, this is accomplished with the execution of the statutorily required agency disclosure form. See CC §2079.17; §§2.31-2.37 on requirements for disclosure and consent of agency relationships in residential transactions.

EXAMPLE: Disclosure must be made, and consent obtained, when a broker represents both the buyer and the seller and intends to receive two separate commissions. *Ohanesian v Watson* (1953) 118 CA2d 386, 257 P2d 1022.

In commercial transactions, written confirmation of the dual agency typically is included in the purchase and sale agreement (or in an earlier letter of intent, should one be used).

A broker may be denied a commission for failing to disclose that a dual agency existed. *L. Byron Culver & Assocs. v Jaoudi Indus. & Trading Corp.* (1991) 1 CA4th 300, 1 CR2d 680. In *Huijers v DeMarrais* (1992) 11 CA4th 676, 14 CR2d 232, a divided court held that a listing agent who gave the statutory agency disclosure to the seller when the purchase contract was signed should have done so before the parties entered into the listing agreement, and that the seller would be entitled to relief from the commission obligation as a remedy for the untimely disclosure.

Some commentators criticize dual agency on the grounds that the conflict between the interests of a buyer and seller are so fundamental that a single broker cannot possibly serve both parties and fulfill the agency obligations of undivided loyalty and full disclosure. See 2 Miller & Starr, California Real Estate §3:12 (3d ed 2002); Bernhardt, *Making the Broker Pay When the Deal Goes Bad*, 29 CEB Real Prop L Rep 242 (Mar 2006). Although these observations are correct, it is also true that the courts have limited dual agency—not prohibited it. *L. Byron Culver & Assocs. v Jaoudi Indus. & Trading Corp., supra*. The broker must disclose and obtain informed consent for the dual agency, but many clients, especially in commercial transactions, find that dual agency can result in more direct negotiations and more clear and comprehensive disclosure. Dual agency can reduce the potential for adversarial posturing that may threaten the making and closing of a deal. Nevertheless, the clients' informed consent to the dual agency is critical in all transactions, and the broker must be alert to the possibility of conflicts. See also discussion of broker's liability for misrepresentation in §§2.140, 2.142, 2.153.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.130 b. Other Multiple Agency Scenarios

§2.130 b. Other Multiple Agency Scenarios

A traditional dual agency (one broker representing both buyer and seller) is not the only situation in which a broker may represent multiple clients with conflicting interests in the same property or transaction. Occasionally a broker may represent more than one potential buyer for the same property. In that situation, however, in contrast to the more common buyer-seller dual agency, there would be no conflict under usual custom and practice unless the competing buyers were represented by the same sales agent. In that case, disclosure and client consent to the multiple agency are required.

EXAMPLE: If two agents in different offices of the same broker each represent a buyer competing for the same property, it is unlikely that either of them, or their common broker, would even know of the conflict. Requiring disclosure in such circumstances would not be practical, and would not provide any meaningful protection to the client's interests.

© The Regents of the University of California

§2.131 c. Self-Dealing

A conflict of interest exists any time a broker (or some third party in a close relationship to the broker) stands to profit personally from the actions taken (or not taken) by the client. As with any other conflict, full and timely disclosure of the facts, and the client's informed consent, are required to avoid a breach of fiduciary duty. See *Savage v Mayer* (1949) 33 C2d 548, 203 P2d 9; Bus & P C §10176(g). But see *Rylander v Karpe* (1976) 60 CA3d 317, 131 CR 415 (loan fee was not profit under listing agreement, was obtained under later, separate agreement not involving sellers, and was taken after sales contract was executed).

© The Regents of the University of California

§2.132 (1) Broker's Purchase of Client's Property: Disclosure Requirements

If the broker purchases the client's property, it will be presumed that the client entered the transaction without sufficient consideration and under undue influence, and the broker will have the burden of proving the fairness of the transaction. *Duffy v Cavalier* (1989) 215 CA3d 1517, 1531, 264 CR 740 (fiduciary duty of broker-agent has same obligations of diligence and faithful service as trustee); *Smith v Zak* (1971) 20 CA3d 785, 98 CR 242 (note that this case cites former CC §2235, which was repealed by Stats 1986, ch 820, §7, operative July 1, 1987; now see Prob C §§16002, 16004). See also Prob C §16463, which requires full disclosure and the principal's consent when a trustee deals with trust property, for duties analogous to those owed by the broker to its client.

The broker may purchase the property if the fact that the broker is purchasing it (and all other facts necessary to fully inform the client) is disclosed to all parties. *Donnellan v Rocks* (1972) 22 CA3d 925, 99 CR 692. Without the required disclosure, the fact that the broker paid a fair price for the property, or that it could not have been sold for a greater price, will not be a defense to liability for nondisclosure. *Bate v Marsteller* (1959) 175 CA2d 573, 346 P2d 903. On the broker's purchase of the principal's property generally, see Comment, *Unprofessional Conduct by Real Estate Brokers: Conflict of Interest and Conflict in the Law*, 11 Pac LJ 821 (1980).

Any fact that might conceivably be material to a transaction must be disclosed by the purchasing broker. The broker's failure to disclose a sale of the listed property to the state for taxes, and the broker's subsequent acquisition of the property, are sufficient to state a cause of action for breach of the broker's fiduciary duty. *Skopp v Weaver* (1976) 16 C3d 432, 128 CR 19.

The broker's duty to disclose all facts relating to the best price obtainable (see §2.138) poses an acute problem for a broker who purchases the client's property for resale. See, *e.g., Smith v Zak, supra*. Resale at a substantial profit will make it difficult for the broker to demonstrate that full disclosure was made. *Smith v Zak, supra*. Any broker who does purchase the client's property should carefully document all disclosures and obtain the client's written acknowledgment and consent.

© The Regents of the University of California

§2.133 (2) Indirect Sales

The duty to disclose the broker's purchase of the listed property extends to purchases by the broker's relatives or employees and entities in which the broker has an interest. In *Batson v Strehlow* (1968) 68 C2d 662, 68 CR 589, a broker's disclosure to the seller that he was president of the purchasing corporation was held inadequate because he did not also disclose that he and his wife were its sole shareholders and had paid the entire price themselves. The broker concealed that he was dealing for himself as principal and attempting to earn a commission as well. A broker should always disclose to the seller any relationship with a buyer corporation or partnership, even if the broker is only a limited partner or minority shareholder.

Brokers also have a duty to disclose that the buyer is a relative or employee. *Smith v Zak* (1971) 20 CA3d 785, 98 CR 242 (buyer was broker's salesperson); *Loughlin v Idora Realty Co.* (1968) 259 CA2d 619, 66 CR 747 (buyer was broker's mother-in-law).

© The Regents of the University of California

§2.134 (3) Broker's Interest in Property Sold to Client

The buyer's broker must fully disclose all benefits the broker will receive from the transaction. A broker must disclose any interest it has in the property being acquired by the client, as well as any interest held by someone related to the broker. The same disclosure obligations and other considerations apply as when a broker purchases the client's property. *Kroeker v Hurlbert* (1940) 38 CA2d 261, 101 P2d 101. If the broker fails to disclose an interest in property that is purchased by the client, the broker must disgorge any profits realized. *Crogan v Metz* (1956) 47 C2d 398, 303 P2d 1029.

© The Regents of the University of California

§2.135 d. Secret Profits

The broker is liable to the principal for any secret profits, gratuities, or other benefits obtained in the transaction. See *Menzel v Salka* (1960) 179 CA2d 612, 4 CR 78. The broker may not retain any benefit derived from the transaction unless the nature and amount of the benefit have been fully disclosed to the principal. It is immaterial that the transaction is otherwise fair to the principal or that the principal receives exactly the desired price for the property or pays no more for it than intended. *Menzel v Salka, supra*. A narrow exception to the requirement of full disclosure of the broker's interest in, and profit from, the sale may arise when the property is sold under a net listing (see §2.61).

The broker must disgorge all secret profits regardless of whether the principal suffered any actual damages. *Savage v Mayer* (1949) 33 C2d 548, 203 P2d 9; see §2.177. The principal may recover from the broker and from all others who knowingly shared in the secret profits (*Crogan v Metz* (1956) 47 C2d 398, 303 P2d 1029), and a fiduciary is liable for secret profits that he or she causes to flow to a third party even if the fiduciary personally does not share in them (*St. James Armenian Church v Kurkjian* (1975) 47 CA3d 547, 121 CR 214).

Brokers are subject to discipline by the Real Estate Commissioner for realizing undisclosed profits as part of a transaction. Bus & P C §10176(g). In *Rylander v Karpe* (1976) 60 CA3d 317, 131 CR 415, a surprising exception to the general rule, it was held that the broker did not violate §10176(g) by accepting loan origination fees from the lender without the sellers' knowledge. *Rylander* appears to be an anomaly. Under Bus & P C §10176(a) it constitutes misrepresentation for a broker for either party in a sale, lease, or exchange who anticipates receiving or receives compensation from a lender in connection with the securing of financing for the transaction, to fail to disclose to both parties before closing, the form, amount, and source of the compensation received or expected. 10 Cal Code Regs §2904.

Kickbacks, referral fees, and other unearned fees from title companies, escrow holders, and the like are prohibited under Bus & P C §10177.4 and the Real Estate Settlement Procedures Act of 1974 (RESPA) (12 USC §§2601-2617), whether disclosed by the broker or not. 12 USC §2607(a)-(b). See §15.95 for discussion of RESPA. Violation of RESPA's ban on kickbacks could subject a broker to criminal penalties as well as civil liability for three times the amount of the referral fee. 12 USC §2607(d). See also *Stetler v Greenpoint Mortgage Funding Inc.* (ED Cal, Jan. 23, 2008) 2008 US Dist Lexis 4880 (court granted summary judgment against claim that mortgage broker failed to disclose alleged kickback payments from a lender because payments were for services rendered—not in violation of RESPA). On kickbacks, referral fees, and other unearned fees from a title company, see California Title Insurance Practice §§1.13-1.14 (2d ed Cal CEB 1997).

© The Regents of the University of California

§2.136 e. The Dishonest Client

A broker is faced with a different type of conflict when the client seeks the broker's participation in conduct that would violate the law or obligations owed by the broker to other parties. This could arise when the client directs the broker not to disclose material information to which the other party is entitled (or requests the broker's assistance in defrauding a lender). The broker is not shielded or relieved from its duty to disclose or to observe the law by the client's instructions to the contrary. Brokers, unlike attorneys, have no client privilege that prohibits disclosure, and no protection from liability for nondisclosure. As a result, there should be no breach of fiduciary duty when the broker makes the required disclosure despite the client's opposition. Withdrawal from the representation may be another option; and a well-drafted commission agreement may still entitle the broker to compensation in such circumstances (see §2.79).

© The Regents of the University of California

§2.137 2. Advice on Price and Value

The scope of the services and advice that the broker provides a client will depend on the type of the transaction and the client's experience and sophistication. A residential seller may expect and need a great deal of help from the broker, while the experienced commercial seller may only need help to find a buyer. For a further discussion of services, see §2.24. The broker's duty as a fiduciary, however, remains the same. If the broker does act, he or she must exercise the standard of care of a fiduciary. On the standard of care, see §2.124.

© The Regents of the University of California

§2.138 a. Best Price Obtainable

An experienced seller may dictate the price to the listing broker, but the broker's advice on the property's fair market value is extremely important for the unsophisticated seller. In such cases the broker, rather than merely suggesting a number, should provide the seller with information regarding comparable sales from which the seller can make a reasonable judgment. The broker must disclose all material facts regarding the value or price of the property, including, when appropriate, the possibility that a higher price might be obtained at a later time or by marketing the property in another way. *Smith v Zak* (1971) 20 CA3d 785, 98 CR 242; *Fisher v Losey* (1947) 78 CA2d 121, 177 P2d 334.

© The Regents of the University of California

§2.139 b. Statements to Parties About Price

In transmitting offers and counteroffers, the broker may be asked to predict a purchase price that the other party will accept. For example, a seller's broker who tells a prospective buyer that the seller is willing to accept less than the asking price may be breaching a fiduciary duty to the seller, unless the seller has authorized such a communication. *Bate v Marsteller* (1959) 175 CA2d 573, 346 P2d 903; *Mitchell v Gould* (1928) 90 CA 647, 266 P 565. On the other hand, generally the seller would not want the broker to discourage a buyer from making any offer below the asking price. The seller can always reject or counter such an offer. A broker's general statement intended to encourage negotiations should be distinguished from the disclosure of confidential information without proper authorization.

© The Regents of the University of California

§2.140 c. Speculative Purchases and Resales

The broker's duties to advise a seller-client regarding price and to assist in obtaining the highest price available do not imply a guarantee that those efforts will be successful. A broker may be liable to a seller if the property is resold at a substantially higher price by a speculator, although the law on the extent of a broker's duty in the area of speculative resales is not settled. The mere existence of a price differential on a subsequent sale would probably not be sufficient to establish either negligence (see §2.159) or breach of fiduciary duty (see §§2.127-2.158), because the price might be the result of recent inflationary increases in property values. An immediate price differential, however, raises the question of whether the broker diligently represented the seller's interest in obtaining the best price for the property.

If the broker is aware that a prospective buyer intends to resell the property shortly at a significantly higher price, disclosure to the seller is required. For an agent who represents both buyer and seller, the agent's failure to disclose to the seller that the buyer is an investor who intends to quickly resell the property constitutes a prima facie case of fraud, misrepresentation, and breach of fiduciary duty. *Jorgensen v Beach 'N' Bay Realty, Inc.* (1981) 125 CA3d 155, 177 CR 882. See also CC §2020; *Rattray v Scudder* (1946) 28 C2d 214, 169 P2d 371 (plaintiff violated fiduciary duty by failing to disclose truth and making misrepresentations about price at which property could be sold).

The seller's broker must also disclose any discussions with the buyer about the possibility of relisting the property with the broker for resale. *Menzel v Salka* (1960) 179 CA2d 612, 4 CR 78. See also *Bay Shore Homes, Inc. v San Diego Trust & Sav. Bank* (1969) 276 CA2d 108, 80 CR 849 (broker denied commission because of failure to disclose agreement to turn over commission to buyer in exchange for listing on resale of property); but see *Moody v Osborne* (1953) 120 CA2d 598, 261 P2d 783 (failure to disclose broker's loan to buyers to enable them to complete transaction did not violate broker's fiduciary duty).

© The Regents of the University of California

§2.141 d. Communicating Offers to Seller

The seller's broker must inform the client of all offers received, regardless of whether they conform to the terms of the listing agreement or whether the broker considers them attractive. Failure to disclose an offer is equivalent to a representation to the seller that no offers were received. *Simone v McKee* (1956) 142 CA2d 307, 298 P2d 667. This duty exists whether the offer is oral or written. *Duin v Security First Nat'l Bank* (1955) 132 CA2d Supp 904, 283 P2d 790. Sound business practice may call for a broker to notify the seller of preliminary negotiations or inquiries even before receipt of a formal offer.

The broker's duty to communicate all offers is owed to the client, and not the other party. Thus, if the seller instructs the broker not to entertain offers below a certain level, the broker has no obligation to the prospective buyer to inform the seller of any nonconforming offer.

© The Regents of the University of California

§2.142 C. Duty to Exercise Reasonable Care

A broker must exercise reasonable skill and care in the performance of services for the benefit of the client (*Schoenberg v Romike Props.* (1967) 251 CA2d 154, 59 CR 359) and is liable for any damages the client suffers because of unreasonable delay or negligence (see *Wilson v Hisey* (1957) 147 CA2d 433, 305 P2d 686). The standard of care is that which would be followed by a competent broker under similar circumstances. In a residential transaction, the standard of care is that of a reasonably prudent broker, which is measured by the degree of knowledge through education, experience, and examination required to obtain a broker's license. CC §2079.2. Professional negligence is the failure to exercise the degree of skill or knowledge ordinarily possessed by an average member of the profession. The applicable standard is not one of perfection, however, and the broker is not a guarantor of the transaction's success. As the court stated in a legal malpractice case, a breach of the duty of care is established not by a mere "failure to be brilliant, but a failure to come up to even a minimum standard of professional competence." *McKnight v Dean* (7th Cir 2001) 270 F3d 513, 518.

In litigation against brokers by clients, it is unusual to see a claim for professional negligence (breach of the duty of care) without accompanying allegations of fraud and breach of fiduciary duty. Thus, reported cases in which breach of the broker's duty of care is addressed are somewhat difficult to analyze because they generally also include and discuss issues of intentional misrepresentation or failure to disclose as well as negligence, and the actual grounds of liability can be difficult to pinpoint. See, *e.g., Ford v Cournale* (1973) 36 CA3d 172, 111 CR 334. The cases discussed in §§2.143-2.147 demonstrate that courts have held brokers to a duty to advise the client correctly and to investigate certain details of the property and the transaction, especially when the principal is unskilled and is relying on the broker's expertise. In the typical residential transaction, where the client is often an unsophisticated consumer relying on the broker for professional expertise in real estate matters, such reliance generally can be presumed. In the context of commercial transactions, where the client's knowledge and experience may equal or exceed the broker's, industry custom and practice is a helpful guideline for the scope of the broker's duty and the client's reasonable reliance.

© The Regents of the University of California

§2.143 1. Advice on Financial Soundness

A broker may be asked for advice on financial issues beyond the listing price. When the broker undertakes to advise the client on such issues as the other party's financial soundness or the security offered, the broker can be held liable if there is a breach of the duty of care. See, *e.g., Pepper v Underwood* (1975) 48 CA3d 698, 122 CR 343, disapproved on other grounds in *Stout v Turney* (1978) 22 C3d 718, 730, 150 CR 637 (negligent misrepresentation that seller's tax returns were consistent with his financial statements); *Banville v Schmidt* (1974) 37 CA3d 92, 112 CR 126 (negligent misrepresentation of value of security under deed of trust and financial strength of obligor on note); *Timmsen v Forest E. Olson, Inc.* (1970) 6 CA3d 860, 86 CR 359 (negligent recommendation of sale to financially unsound buyer).

The broker is not a guarantor of the financial success of the client's investment. The broker should establish a clear understanding with the client regarding the scope of services to be performed. For example, if the client is purchasing a property and the rental income from a particular tenant is essential to the success of the investment, the broker is not required to conduct its own investigation of the tenant's financial condition. However, unless the client has the experience to understand the importance of such an inquiry, the broker should at least inform the client that it should be done, with the assistance of the appropriate professional advisor (*e.g.,* an accountant). If the broker does undertake the task of performing financial due diligence, it must do so competently. See *Bank of America v J. A. Williams* (1948) 84 CA2d 562, 191 P2d 17**.**

© The Regents of the University of California

§2.144 2. Advice on Title Matters

Brokers may also breach their duty of care by failing to investigate, or failing to advise the client to investigate, matters regarding title. In *Brady v Carman* (1960) 179 CA2d 63, 3 CR 612, a broker was held liable for erroneously advising a buyer that an easement across the property did not affect its value. In *Wilson v Hisey* (1957) 147 CA2d 433, 305 P2d 686, a broker's failure to recommend a title search was negligent when he had erroneously stated that there was only one encumbrance on the property. In *Pepitone v Russo* (1976) 64 CA3d 685, 134 CR 709, a broker was held liable for failing to advise the principal of a due-on-sale clause in a second deed of trust.

© The Regents of the University of California

§2.145 3. Advice on Real Estate Matters

Brokers represent themselves to the public as having particular knowledge and skills in the real estate field and are under a corresponding obligation to exercise greater care and skill than is within the capacity of ordinary citizens. *Richards Realty Co. v Real Estate Comm'r* (1956) 144 CA2d 357, 300 P2d 893. Brokers must meet certain educational requirements (Bus & P C §§10153.3-10153.5) and must update their professional knowledge through continuing professional education (Bus & P C §§10170-10171.5). In addition, they must pass an examination prepared and administered by the state, which tests, among other things, their knowledge of real property law and legal principles. Bus & P C §10153.

© The Regents of the University of California

§2.146 4. Advice on Tax Considerations

Brokers may be liable if they advise clients on tax considerations and do so incorrectly. In *Santos v Wing* (1961) 197 CA2d 678, 17 CR 457, the broker escaped liability for his alleged failure to give advice on the tax consequences of a transaction, because he had advised his principal to seek the advice of an attorney on the question. The broker will not be liable for failing to give tax advice if the contractual documents between the client and broker specifically admonished the client to get tax advice elsewhere. Moreover, such an admonition does not violate public policy, because the legislature has decided that clients should get tax advice from professionals other than real estate brokers. *Carleton v Tortosa* (1993) 14 CA4th 745, 17 CR2d 734. See CC §2079.16 (requiring disclosure to client that "[i]f legal or tax advice is desired, consult a competent professional").

© The Regents of the University of California

§2.147 5. Advice on Legal Matters

There is a lack of reported case authority on the extent of legal competence required of brokers, but they will incur liability for negligently giving legal advice to their clients or for negligently drafting legal documents. See, *e.g., Biakanja v Irving* (1958) 49 C2d 647, 320 P2d 16, in which a notary public was held liable for negligence in drafting a will. In *People v Sipper* (1943) 61 CA2d Supp 844, 142 P2d 960, disapproved on other grounds in *Murgia v Municipal Court* (1975) 15 C3d 286, 124 CR 204, a real estate broker (not involved in the sale or purchase of property) who prepared, for a fee, a document to secure a loan with real property was held liable for the unauthorized practice of law in violation of Bus & P C §6125. The court held that the practice of law includes "legal advice and counsel and the preparation of legal instruments and contracts by which legal rights are secured." 61 CA2d at 846.

There is no clear definition of what constitutes "basic" real estate legal principles that a broker should understand, or when the line is crossed into the unauthorized practice of law. The cases at either extreme may be easy to identify, but there is a sizeable gray area in between. In evaluating the broker's conduct, the following points must be kept in mind: The broker (1) is not authorized to offer legal advice, but (2) should inform the client when outside legal advice is needed (see Miller & Starr, California Real Estate §3:26 (3d ed 2002)), and (3) will be responsible for the advice it does provide. *Biakanja,* 49 C2d at 647.

© The Regents of the University of California

§2.147A 6. Advice on Short Sales

A short sale is an example of an area that may require advice beyond the expertise of a real estate agent or broker. In a recessionary market, a homeowner or real estate investor may be faced with the serious challenge of value shrinking to less than the outstanding loan balance at the same time as interest rates and mortgage payments are rising beyond the owner's means. A short sale may be the best of the available options. A short sale may involve, among other things, knowledge of accounting, taxation, and alternative ways to structure the transaction for the client's needs. The licensee is not expected to have the skill and training to advise on such issues, but is expected to inform the client of the limitations of his or her knowledge and to recommend that the client seek the advice of an appropriately trained lawyer or other professional. An agent who goes beyond his or her area of expertise will be held to the requisite standard of competence and thus risks being negligent or even crossing into the unauthorized practice of law. See *Carleton v Tortosa* (1993) 14 CA4th 745, 17 CR2d 734 (broker informed client to seek advice from tax counsel on any tax issues); *Santos v Wing* (1961) 197 CA2d 678, 17 CR 457 (broker urged seller to seek tax counsel). On short sales, see §§6.106C-6.106F; on distressed sales generally, see §§6.106A-6.111.

© The Regents of the University of California

§2.148 D. Duty to Perform With Diligence

The seller can revoke an exclusive agency or exclusive right-to-sell listing if the broker fails to diligently carry out the terms of the agency. *Coleman v Mora* (1968) 263 CA2d 137, 69 CR 166. (An open listing is generally characterized as a unilateral offer that the seller may revoke regardless of the broker's diligence. See §2.59.) The broker's lack of diligence will constitute a defense to his or her action for payment of a commission if the seller revokes the listing before accepting an offer procured by anyone other than the broker. In *Coleman,* the court of appeal held that the principal may revoke a listing agreement for any of the reasons for which contracts may generally be revoked (see CC §1689 for grounds for rescission), including failure to perform. The broker's breach alone does not terminate the listing agreement, however, and to avoid liability for the commission the seller should clearly exercise the right to revoke before the property is sold. See *Whitney Inv. Co. v Westview Dev. Co.* (1969) 273 CA2d 594, 78 CR 302.

Whether the broker has performed with diligence is a question of fact to be decided in light of the circumstances of each case. *Whitney Inv. Co. v Westview Dev. Co., supra*. A seller must be careful in exercising the right to revoke, because if the listing is terminated without adequate cause, the broker may be entitled to the commission without any further performance, especially if the listing agreement contains a withdrawal-from-sale clause (see §2.114). *Blank v Borden* (1974) 11 C3d 963, 115 CR 31.

PRACTICE TIP: The need for adequate cause underscores the importance to the seller of specifying in the listing agreement the services the broker is to perform. See §2.84. It will be easier to establish a breach if the broker's duties were stated in detail and if the broker is notified of the seller's dissatisfaction (and has an opportunity to cure its performance) before termination.

© The Regents of the University of California

§2.149 E. Duty to Account

The broker must account for all funds held on the client's behalf and cannot commingle the client's funds with personal funds. Bus & P C §10176(e). See also *Brown v Gordon* (1966) 240 CA2d 659, 49 CR 901 (revocation of license based on commingling of funds). The broker holds the client's funds as trustee and is responsible for their disposition in accordance with the client's directions. *Holloway v Thiele* (1953) 116 CA2d 68, 253 P2d 131.

The broker may be called on to receive and hold the buyer's deposit as agent for the buyer, as agent for the seller, or as escrow holder under written instructions in the offer or contract. See §§2.67-2.70. The Real Estate Law (Bus & P C §§10000-10580) and regulations adopted by the Real Estate Commissioner (10 Cal Code Regs §§2700-3109) limit the circumstances in which a broker may receive and hold a deposit check before the offer is accepted; they generally require the deposit to be placed in escrow or in the broker's trust account no later than 3 business days after receipt. Bus & P C §10145; 10 Cal Code Regs §2832. A broker may hold funds uncashed only with the seller's written permission. 10 Cal Code Regs §2832. One shortcoming of using preprinted real estate purchase contracts is the implied requirement that a deposit accompany the initial offer. Many brokers and prospective buyers interpret this form as requiring delivery of a check to the broker long before the parties have reached agreement, although the seller's interest would be adequately protected by a deposit at the time the purchase agreement is executed. See §§2.69-2.70.

The DRE regulates brokers' trust funds generally and imposes various recordkeeping requirements on brokers. Bus & P C §10145; 10 Cal Code Regs §§2830.1-2836. A broker must provide quarterly accountings to the client of any advance fees that the broker holds for the client. Bus & P C §10146. In *Burch v Argus Props.* (1979) 92 CA3d 128, 154 CR 485, the client was permitted to recover the amount of fees advanced, as punitive damages, for the broker's failure to render quarterly accountings as required by Bus & P C §10146, even though the funds had been returned to the client before the action was commenced.

© The Regents of the University of California

F. Limitations on Broker's Duties

§2.150 1. No Duty to Verify Accuracy of Others' Representations

Although a broker is not required to independently verify the accuracy of another party's representations, it is important that the client know whether the information communicated by the broker *has* been confirmed or is merely being forwarded from another source without verification. In *Salahutdin v Valley of Cal., Inc.* (1994) 24 CA4th 555, 29 CR2d 463, the broker knew that the buyers wanted property that could be subdivided and that only parcels of one acre or more could be subdivided. The broker relied on (1) a disclosure in the multiple listing sheet that the property in question contained an acre and (2) a personal inspection that showed a fenced area that contained an acre. The actual property purchased by the buyers contained only 0.998 acres and could not be subdivided. The broker's liability was not founded on a breach of the duty to inspect and disclose (see CC §§2079-2079.6, 2079.12; *Easton v Strassburger* (1984) 152 CA3d 90, 199 CR 383), but rather on a breach of the fiduciary duty not to make representations of material facts to a client without advising the client that the broker is merely passing on information received from the seller without verifying its accuracy. In *Robinson v Grossman* (1997) 57 CA4th 634, 67 CR2d 380, however, the court ruled that a listing agent's statutory duty to disclose material facts does not include a duty to verify or disclaim sellers' potentially inaccurate statements. If the client reasonably believes that the information the broker provides is the result of the broker's own independent investigation, the broker will be held accountable for its accuracy; but if it is reasonably clear that the information came from some other source (*e.g.,* the seller or a public record), the broker should not be considered a guarantor of the accuracy of the information by merely passing it on to the client. To avoid dispute, the broker should disclose to the client the source of the information.

© The Regents of the University of California

§2.151 2. No Duty to Advise on Matters Outside of Broker's Expertise

A broker is expected to possess a certain basic level of knowledge regarding real estate matters generally, and a higher level of knowledge if it promotes itself as an expert in some particular area of real estate. A transaction can involve many issues that are outside the scope of the typical broker's expertise; some, such as legal issues, tax matters, accounting issues, construction, engineering, and hazardous materials, require the assistance of other professionals. One or more these areas may be crucial to a particular transaction, but each requires experience and training beyond that of the average real estate broker. See, for example, §§2.146-2.147.

The broker is not obligated to provide advice in subjects outside its core real estate expertise. A broker, however, may be expected to recognize when an issue requires analysis by another professional, in which case there is a duty to inform the client that such a person should be consulted. See *Carleton v Tortosa* (1993) 14 CA4th 745, 17 CR2d 734. Finally, if the broker attempts to advise in one of these other areas (without appropriate disclaimer and recommendation that more professional advice be obtained), the broker will be not be excused if its advice is incorrect or incomplete.

© The Regents of the University of California

VII. CLAIMS AGAINST BROKER

§2.152 A. Breach of Fiduciary Duty

Brokers are subject to two separate and distinct areas of liability for violating their fiduciary duties. Brokers may incur civil liability to the principal under various causes of action (see §§2.124-2.151). Brokers also are subject to disciplinary proceedings before the Real Estate Commissioner under Bus & P C §§10175-10185. See §§2.171-2.174. An aggrieved party may maintain both administrative and legal actions simultaneously. In addition, a real estate agent is liable under CC §51.9 for sexual harassment of a client.

On claims against brokers and on defending brokers, see California Real Estate Brokers: Law and Litigation, chaps 5, 8-9 (Cal CEB 2009); on brokers' error and omission and liability insurance, see RE Brokers, chap 10; on litigating against brokers, see RE Brokers, chaps 11-12.

© The Regents of the University of California

§2.153 1. Bases of Liability

Both common law and statutory law provide bases of liability for a broker's breach of a fiduciary duty. Under the common law, a broker who breaches the contract with the principal is liable under general contract law, entirely apart from the law of agency. *Anderson v Badger* (1948) 84 CA2d 736, 191 P2d 768. In addition to contractual rights against the broker, the principal—in both residential and commercial transactions—may find the following common law remedies available under theories of fraud, breach of fiduciary duty, misrepresentation, concealment, deceit, third party tort, and negligence:

- Damages for losses suffered from the broker's breach of fiduciary duty (see §§2.127-2.158);
- Damages for the broker's negligence (see §2.159);
- Recovery of the broker's secret profits (see §2.160);
- Recovery of the broker's commission (see §2.161);
- Punitive damages (see §2.162); and
- Indemnity for damages recovered from the principal by third parties and/or attorneys fees incurred in prosecuting or defending against third party claims (see §2.163).

The court in *Easton v Strassburger* (1984) 152 CA3d 90, 199 CR 383, held that a residential broker has the affirmative duty to conduct a reasonably competent and diligent inspection of the property. The legislature later codified this duty. CC §§1102-1102.17, 2079-2079.24. See §§2.133-2.134. The enactment of these statutes did not diminish the common law responsibilities of commercial brokers and residential brokers, but rather created an additional statutory duty for residential brokers, who can now be found liable under theories of fraud, breach of fiduciary duty, misrepresentation, concealment, and deceit for breach of their duties to conduct a reasonably diligent inspection and to disclose anything that would affect the value or desirability of the property.

NOTE: The statutory duties imposed on brokers by CC §§1102-1102.17 and 2079-2079.24 and the cases interpreting these sections apply only to residential—not commercial—real estate transactions. Practitioners analyzing a broker's duty in a failed residential transaction must take great care to distinguish and analyze both the common law and statutory theories of liability. These duties are not mutually exclusive. In litigation involving residential transactions, the potential theories of liability under the common law and under the statutes should be appreciated as distinct and parallel bases for separate and distinct liability. Although the theories are legally distinct, the respective rights may overlap. For instance, even before enactment of CC §§1102-1102.17 and 2079-2079.24, brokers were under a general duty to disclose any material defects in a property. *Lingsch v Savage* (1963) 213 CA2d 729, 29 CR 201.

For an excellent explanation of how the statutory duties under CC §2079 can differ from the broader fiduciary duties of an agent, see *Michel v Moore & Associates, Inc.* (2007) 156 CA4th 756, 67 CR3d 797. In *Michel,* a secondary agent, Kirkpatrick, who worked for the cooperating broker, had inspected a home and taken notes of the property's defects. Kirkpatrick's associate, Lagudis, who also worked for the cooperating broker, represented plaintiff-buyers. Lagudis prepared a transfer disclosure statement which did not include certain items in Kirkpatrick's notes. Kirkpatrick reviewed the transfer disclosure statement but did not augment it or tell Lagudis about the other defects he had found. In reversing dismissal of the negligent nondisclosure cause of action against the cooperating broker, the court noted the cause involved elements different from the buyers' §2079 and fraudulent concealment causes of action. The fiduciary duty owed by brokers to their clients was substantially more extensive than the nonfiduciary duty codified in §2079. 156 CA4th at 762.

© The Regents of the University of California

§2.153A 2. Pre-Litigation and Pre-Arbitration Duty to Mediate

Many residential purchase agreements include a requirement to mediate before resorting to litigation or arbitration. These provisions routinely preclude recovery of attorney fees if the prevailing party did not make a good faith effort to mediate or refused to mediate after a request was made. In *Frei v Davey* (2004) 124 CA4th 1506, 1508, 22 CR3d 429, the court construed such a provision literally and concluded that it "means what it says and will be enforced." See also *Lange v Schilling* (2008) 163 CA4th 1412, 78 CR3d 356 (same, quoting *Frei*).

© The Regents of the University of California

§2.154 3. Right to Arbitrate Claims

Whether claims against a broker can or must be arbitrated may depend not only on a written contract between the broker and principal, such as a listing agreement or commission agreement, but also may be based on the purchase and sale agreement between the seller and buyer if the broker is deemed to be a party to such agreement.

PRACTICE TIP: Practitioners handling either residential or commercial disputes should obtain and marshal all documents and facts in a chronological fashion as quickly as possible in the early stages of the dispute. With this technique, if an earlier-signed agreement has been modified in any manner by later-signed documents, it will quickly stand out. For instance, rights of the principals or the brokers may have been added or deleted in later-executed documents between the same parties. The executed purchase agreement may provide for attorney fees and expressly allow the broker to rely on that provision, whereas the earlier listing agreement included no such provision. Similarly, the listing or commission agreement may provide for the broker to be paid a certain percentage commission that is later expressly modified in writing.

In *Westra v Marcus & Millichap Real Estate Inv. Brokerage Co.* (2005) 129 CA4th 759, 28 CR3d 752, the broker was not a party to the purchase and sale agreement, but was nevertheless entitled to enforce the arbitration provision in that agreement as the agent of the signatories to the agreement. In addition, the federal Arbitration Act (9 USC §§1-16) may preempt state arbitration laws when federal financing is contemplated and forms supplied by a national organization are used in the transaction. *Hedges v Carrigan* (2004) 117 CA4th 578, 583, 11 CR3d 787; see also *Westra,* 129 CA4th at 764. But see *Nguyen v Tran* (2007) 157 CA4th 1032, 1038, 68 CR3d 906, in which the court both followed and distinguished *Westra*. It concluded that the cooperating brokers, as agents of a signatory to the purchase agreement, could compel the buyers to arbitrate under the arbitration clause in the purchase agreement signed solely by the buyers and the sellers but could not, as nonsignatories, compel another nonsignatory, the listing broker, to arbitrate.

© The Regents of the University of California

§2.155 4. Damages for Breach of Fiduciary Duty

A breach of the broker's fiduciary duty, whether intentional or negligent, makes the broker liable to the principal for damages caused by the breach. See §§2.124-2.126 on breach of fiduciary duty. See also *Warren v Merrill* (2006) 143 CA4th 96, 49 CR3d 122. However, the appropriate measure of damages for such breach is unclear, and the principal's recovery may vary a great deal, depending on the measure used. Confusion exists because the cases dealing with breach have used terms such as "benefit of the bargain" imprecisely and because the rules articulated in cases involving breach of contract, fraud, and unjust enrichment have been applied to inappropriate fact situations. See *Overgaard v Johnson* (1977) 68 CA3d 821, 137 CR 412, for an analysis of these conflicting rules. Naturally, the principal will want to frame a lawsuit for breach of fiduciary duty in terms that will bring the case under the broadest possible measure of damages, while the broker will seek to invoke the most restrictive measure.

Under the benefit-of-the-bargain standard, the principal is entitled to recover the difference between the actual value of the property and the value the principal expected to receive, while an out-of-pocket measure would permit recovery only of the difference between the actual value of the property and the amount paid. In between is the loss-of-profits measure, recognized by the California Supreme Court in *Stout v Turney* (1978) 22 C3d 718, 150 CR 637, which permitted recovery of incidental costs and expenses in recovering secret profits that the broker had obtained in the transaction. See, *e.g., Ward v Taggart* (1959) 51 C2d 736, 336 P2d 534; *Simone v McKee* (1956) 142 CA2d 307, 298 P2d 667. See §2.135 on secret profits.

The benefit-of-the-bargain standard is applied if the plaintiff's action against a broker, as a fiduciary, establishes intentional misrepresentation. See *Fragale v Faulkner* (2003) 110 CA4th 229, 235, 1 CR3d 616 (measure of damages in case of intentional misrepresentation by fiduciary is not limited to out-of-pocket losses).

An extended discussion of the measure of damages for breach of fiduciary duty is contained in *Salahutdin v Valley of Cal., Inc.* (1994) 24 CA4th 555, 29 CR2d 463, discussed in §2.150. The appellate court in *Salahutdin* noted that there was an apparent split of authority on the issue but adopted the broader benefit-of-the-bargain measure of damages under CC §§1709 and 3333. See also *Strebel v Brenlar Investments* (2006) 135 CA4th 740, 37 CR3d 699, in which the court chose not to adopt either the benefit-of-the-bargain or the out-of-pocket loss rule, and allowed the plaintiff to fully recover for all injuries suffered under CC §3333. In allowing the plaintiff to recover appreciation damages incurred after the date of the fraud, the court rejected a formulaic approach and appeared to take a broader, equitable approach to ensuring that the victim of the fraudulent conduct received a full, equitable, and logical recovery.

© The Regents of the University of California

§2.156 a. Breach of Contract; Fraud Actions

For breach of contract actions, the measure of damages is governed by CC §3300, which authorizes recovery under a benefit-of-the-bargain standard. In fraud cases, recovery is limited to out-of-pocket losses, or to lost profits if the principal acquired the property for profit or gain. CC §3343. Lost profits are unavailable if the property was purchased for residential purposes. See *Stout v Turney* (1978) 22 C3d 718, 728 n12, 150 CR 637.

© The Regents of the University of California

§2.157 b. Tort Action

For breach of fiduciary duty, including fraudulent breach, the tort measure of damages of CC §3333 applies. Section 3333 provides for recovery of an amount that will "compensate for all the detriment proximately caused" by the breach, but it does not include the benefit-of-the-bargain language of CC §3300. *Overgaard v Johnson* (1977) 68 CA3d 821, 137 CR 412.

The recovery formula to be applied under CC §3333 is unsettled. Some courts have held that the measure of damages under §3333 is the benefit-of-the-bargain rule that applies to actions for breach of contract under CC §3300. *Pepitone v Russo* (1976) 64 CA3d 685, 134 CR 709; *Pepper v Underwood* (1975) 48 CA3d 698, 122 CR 343, disapproved on other grounds in *Stout v Turney* (1978) 22 C3d 718, 730, 150 CR 637. A benefit-of-the-bargain standard for breach of fiduciary duty is provided for in CACI 1924.

In *Fragale v Faulkner* (2003) 110 CA4th 229, 1 CR3d 616, the court distinguished between intentional and negligent misrepresentation by a fiduciary. Citing dictum in *Alliance Mortgage Co. v Rothwell* (1995) 10 C4th 1226, 44 CR2d 352, the court held that the purchasers of a home would be entitled to recover the cost of repairing code violations if they prevailed in their claim that their broker intentionally misrepresented that additions to the home were built to code; if they proved only negligent misrepresentation, however, they would be limited to an out-of-pocket measure. See also, CACI 1924, citing and quoting *Alliance Mortgage Co. v Rothwell, supra*. Other courts have held that §3333 limits the principal's recovery to the extent of the financial injury actually sustained and is not a benefit-of-the-bargain measure. *Ward v Taggart* (1959) 51 C2d 736, 336 P2d 534; *Walters v Marler* (1978) 83 CA3d 1, 147 CR 655; *Overgaard v Johnson, supra*. See also California Attorney's Guide to Damages §2.35 (2d ed Cal CEB 2004).

In *Overgaard v Johnson, supra,* the seller listed farm property for sale. The broker found a buyer but negligently failed to advise the buyer that the amount of the acreage for sale was less than that stated in the sale documents. The buyer recovered from the seller the difference between the sale price and market value, and the seller then sued the broker for that amount plus attorney fees. The court of appeal held that under CC §3333 the seller was entitled to recover brokerage fees on the price differential and to recover attorney fees, but the seller could not recover the price differential itself because §3333 does not provide for a benefit-of-the-bargain standard.

© The Regents of the University of California

§2.158 c. Attorney Fees

A broker who commits a fraudulent breach of fiduciary duty is not liable for the defrauded party's attorney fees unless there is an applicable exception to the general rule that each party bears its own attorney fees. *Gray v Don Miller & Assocs.* (1984) 35 C3d 498, 198 CR 551. In so holding, the *Gray* court disapproved the portion of *Walters v Marler* (1978) 83 CA3d 1, 147 CR 655, that upheld a fee award, but did find a partial exception in holding that the buyer's attorney fees incurred in a specific performance action against the seller (brought in reliance on the broker's misrepresentation) were recoverable. The court's rationale was that the buyer had sued the seller based on the "third party tort" of the broker. See also *Behniwal v Mix* (2005) 133 CA4th 1027, 35 CR3d 320 (sellers' broker was sued on "third party tort theory" and prevailed against claim for attorney fees after it was found that sellers had ratified forged counteroffer signed by sellers' broker); *Heckert v MacDonald* (1989) 208 CA3d 832, 256 CR 369 (attorney fees on "third party tort theory" were denied because seller had received more than amount in question through increase in sale price arising from broker's wrongful activities).

A broker who successfully defended against his client's fraud and rescission claim was *not* entitled to attorney fees in *Super 7 Motel Assocs. v Wang* (1993) 16 CA4th 541, 20 CR2d 193. To take advantage of an attorney fee clause, the claimant usually must be a party to the contract, and the *Super 7* broker was neither a party nor a third party beneficiary of the contract. A defendant who is not a party to a contract may sometimes be entitled to fees if the plaintiff would have been able to recover them had he or she prevailed. Because the client's fraud claim against the broker in *Super 7* was really an ancillary tort claim, not a contract claim, however, the client would not have been able to recover attorney fees from the broker and, reciprocally, the broker could not recover them from the client.

In *Hasler v Howard* (2004) 120 CA4th 1023, 1027, 16 CR3d 217, the wording of the attorney fees provision was pivotal; the court stated: "Instead of covering any action or lawsuit arising from the listing agreement, the provision here only applies to actions 'regarding the obligation to pay compensation' under the listing agreement…." A tort action for fraud, breach of fiduciary duty, and breach of duty to disclose did not satisfy the explicit language in the listing agreement. But see *Pacific Preferred Props. v Moss* (1999) 71 CA4th 1456, 84 CR2d 500, in which the court, on the basis of references to the broker in various sections of the purchase contract, found that the broker was a party to the contract and awarded attorney fees to the prevailing-party seller. For discussion of fees in action between buyer and seller, see §4.140.

In *Xuereb v Marcus & Millichap, Inc.* (1992) 3 CA4th 1338, 5 CR2d 154, the court was faced with defendants who had prevailed on tort causes of action at trial but had been denied recovery of their attorney fees and costs under the contract. In overturning the ruling on attorney fees, the court noted that the attorney fee provision allowed fees and costs to the prevailing party if a suit or other legal proceeding arose from the agreement. The language was broad enough to encompass both contract and tort claims.

For a good discussion analyzing "prevailing party," see *Wakefield v Bohlin* (2006) 145 CA4th 963, 52 CR3d 400.

© The Regents of the University of California

§2.159 B. Damages for Negligence

Generally speaking, a person rendering services is liable for negligence if the damage or injury is foreseeable. *Biakanja v Irving* (1958) 49 C2d 647, 320 P2d 16. This rule applies to real estate brokers with respect to their duties toward principals in a transaction, whether or not they are in contractual privity. *Merrill v Buck* (1962) 58 C2d 552, 25 CR 456; *Easton v Strassburger* (1984) 152 CA3d 90, 199 CR 383. The measure of damages in agency situations is all damages proximately caused by the negligence. CC §3333; *Smith v Rickard* (1988) 205 CA3d 1354, 254 CR 633.

PRACTICE TIP: Although attorney fees are seldom recoverable in negligence actions, the decision in *Perry v Robertson* (1988) 201 CA3d 333, 247 CR 74, is an example of the court's liberal treatment of a pleading that asserted both contract and negligence theories because the broker's misdrafting of a contract resulted in an inadequate sale price. The basis for the attorney fees award was a clause in the listing agreement, and the court held that, because the remedy sought and obtained was the same under either theory, the trial court had properly awarded the fees based on a contract theory. This case underscores the importance of the selection of causes of action.

For discussion of attorney fee awards in tort actions between buyers and sellers, see §4.140.

© The Regents of the University of California

§2.160 C. Recovery of Secret Profits

A broker who obtains secret profits must return them to the principal on the theory that all profits in the transaction, without full disclosure and a specific agreement to the contrary, belong to the principal. *Menzel v Salka* (1960) 179 CA2d 612, 4 CR 78. See §2.135. The duty extends to persons with whom the broker has no fiduciary relationship and with whom the broker deals at arm's length. *Ward v Taggart* (1959) 51 C2d 736, 336 P2d 534.

The broker must disgorge all secret profits, not because of injury to the principal, but because all benefits and advantages gained by the agent go to the principal. *Savage v Mayer* (1949) 33 C2d 548, 203 P2d 9. The remedies typically used by plaintiffs to recover secret profits are imposition of a constructive trust or an equitable lien. *St. James Armenian Church v Kurkjian* (1975) 47 CA3d 547, 121 CR 214. When the funds have been dissipated, however, an award of money damages is proper. *St. James Armenian Church v Kurkjian, supra*.

Even if the broker receives no secret profits, if they flow to a third party because of the broker's breach of fiduciary duty, the broker is liable to the principal for those profits. *St. James Armenian Church v Kurkjian, supra*. The principal may be entitled to rescind the transaction if the wrongful conduct is discovered before the conveyance occurs. *Rodes v Shannon* (1963) 222 CA2d 721, 35 CR 339.

© The Regents of the University of California

§2.161 D. Recovery of Commission

If the broker's breach of fiduciary duty was willful, the principal may be entitled to recover the commission. *Sierra Pac. Indus. v Carter* (1980) 104 CA3d 579, 163 CR 764; *Menzel v Salka* (1960) 179 CA2d 612, 4 CR 78. If the breach is merely negligent, the injured party is entitled to actual damages but the broker does not forfeit the commission. *Ziswasser v Cole & Cowan, Inc.* (1985) 164 CA3d 417, 425, 210 CR 428.

© The Regents of the University of California

§2.162 E. Punitive Damages

Punitive damages may be awarded if it is shown, by clear and convincing evidence, that the broker's misconduct was oppressive, fraudulent, or malicious. CC §3294; *Haigler v Donnelly* (1941) 18 C2d 674, 117 P2d 331; *Simone v McKee* (1956) 142 CA2d 307, 298 P2d 667. Punitive damages are unavailable for breach of contract—even if the breach is willful and even if the contract creates the fiduciary obligation. CC §3294; *Crogan v Metz* (1956) 47 C2d 398, 303 P2d 1029. They may be available, however, for breach of fiduciary duty (a noncontract claim) on proof of oppression, fraud, or malice. CC §3294.

The standard for misconduct may differ depending on whether the broker has a fiduciary or nonfiduciary relationship with the plaintiff, and is entirely determined by the factual circumstances. Depending on those factual circumstances, a broker may incur punitive damages for behavior less flagrant than would justify their award against either a nonprofessional or a nonfiduciary. See, *e.g., Ward v Taggart* (1959) 51 C2d 736, 336 P2d 534.

© The Regents of the University of California

§2.163 F. Indemnity

The principal is entitled to implied indemnity from the broker for damages recovered by third parties because of the broker's actions. *Walsh v Hooker & Fay* (1963) 212 CA2d 450, 28 CR 16; *Kruse v Miller* (1956) 143 CA2d 656, 300 P2d 855. See *Overgaard v Johnson* (1977) 68 CA3d 821, 137 CR 412, discussed in §2.157, on the measure of damages in an indemnity situation. See also *Trust One Mortgage Corp. v Invest Am. Mortgage Corp.* (2005) 134 CA4th 1302, 37 CR3d 83, in which the broker was liable to the lender under a written indemnity provision that did not violate the antideficiency laws.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.164 G. Recovery of Unsatisfied Judgments From Recovery Account of Real Estate Fund

§2.164 G. Recovery of Unsatisfied Judgments From Recovery Account of Real Estate Fund

The Real Estate Law (Bus & P C §§10000-10580) provides for a special fund (called the Recovery Account, a component of the Real Estate Fund) from which any aggrieved person may satisfy a judgment against a real estate licensee for fraud, misrepresentation, deceit, or conversion. Bus & P C §§10450.6, 10470-10481.

NOTE: A judgment against a licensee is defined as a final judgment in a court of competent jurisdiction, including a federal court, but not a court of another state. Bus & P C §10471(a).

Recovery is also allowed from the Recovery Account following an arbitration award that has been confirmed and reduced to judgment under CCP §1287.4. Bus & P C §10471.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/ 1. Requirements for Recovery/§2.165 a. Licensed Defendant

1. Requirements for Recovery

§2.165 a. Licensed Defendant

The defendant must have been licensed as a broker or a salesperson under the Real Estate Law (Bus & P C §§10000-10580) at the time the misconduct occurred. Bus & P C §10471. See *Powers v Fox* (1979) 96 CA3d 440, 158 CR 92. For the Recovery Account (see §2.164) to be liable, the transaction that gave rise to the plaintiff's claim must have been one for which a real estate license is required (Bus & P C §10471); recovery is not permitted if the broker was acting on his or her own behalf. See *Robinson v Murphy* (1979) 96 CA3d 763, 158 CR 246 (defendant not acting as broker when selling own property); *McGaughey v Fox* (1979) 94 CA3d 645, 156 CR 593 (not acting as broker when selling own share and not acting on behalf of partnership).

© The Regents of the University of California

§2.166 b. Basis of Judgment

A petition to recover from the Recovery Account will not be granted unless the judgment arose out of fraud, misrepresentation, deceit, or the conversion of trust funds and the broker had the requisite intent to defraud. Bus & P C §10471. The trial court's decision creates a rebuttable presumption of the fraud, misrepresentation, deceit, or trust fund conversion on which the action against the Recovery Account is based. Thus, to this limited extent, the licensee has an opportunity to legally justify why the judgment was in error or why the licensee did not commit fraud. The trial court's findings are conclusive on the licensee, however, as to any other issues. *Deas v Knapp* (1981) 29 C3d 69, 171 CR 823. Although the DRE is not bound by the trial court's findings, it must overcome a rebuttable presumption on all issues. The burden of proof is on the applicant if the judgment was by default, stipulation, or consent under CCP §594, or if the licensee was defended by a trustee in bankruptcy. Bus & P C §10473. The applicant's claim against the Recovery Account must be based on the statutorily approved grounds; even if the licensee was found liable in the trial court on other grounds, they cannot be asserted against the Recovery Account. *Stuart v Department of Real Estate* (1983) 148 CA3d 1, 195 CR 524. For instance, in *Yergan v Department of Real Estate* (2000) 77 CA4th 959, 92 CR2d 189, the applicants were not entitled to payment when the stipulated judgment and underlying settlement were based on the licensee's professional negligence and not on a statutorily approved ground.

© The Regents of the University of California

§2.167 c. Specified Categories of Actions

Recovery is allowed for specified categories of actions (see §2.166), as long as the action arises "directly out of any transaction in which the defendant, while licensed under [the Real Estate Law], performed acts for which a real estate license was required." Bus & P C §10471(a). This provision appears to codify the reasoning in *Merrifield v Edmonds* (1983) 146 CA3d 336, 194 CR 104, in which an action against a real estate salesperson for failure to repay two personal loans was found not to have arisen "directly" from a real estate transaction, and recovery from the fund was denied. Similarly, a judgment for losses arising from the salesperson's nonresident property management was not recoverable from the fund because the salesperson was not licensed to perform such work. The court held that, under former Bus & P C §10471, the claimant's loss must derive from a transaction in which the judgment debtor performed acts that required a license, in this case a broker's license. In *Merrifield,* the nonresident property management contract was invalid because the salesperson was not a licensed broker. Therefore, the court reasoned, the judgment creditor was not protected by the fund as an "innocent member of the public," because he entered into an illegal contract with the salesperson. The court noted that under Bus & P C §10138 the judgment creditor committed a misdemeanor by paying the salesperson.

Merrifield was distinguished in *Vinci v Edmonds* (1986) 185 CA3d 1251, 230 CR 308, in which a licensed salesperson misrepresented that he was a licensed broker and defrauded the plaintiffs in a short-term swing loan transaction for which a broker's license is required. Although the salesperson was not properly licensed for the acts performed, the *Vinci* court held the plaintiffs to be innocent members of the public, who were within the class of individuals that the Recovery Account was intended to benefit. The court found that the plaintiffs in *Vinci* had been deceived about the salesperson's status and were free of any wrongdoing themselves, unlike the plaintiff in *Merrifield*, who knew the status of the salesperson and knew that it was wrong to pay him. It appears that a ruling like the one in *Vinci* will be precluded in the future by the 1987 amendment to Bus & P C §10471(a), which requires, as a condition of recovery, that the transaction not be in violation of Bus & P C §10137 or §10138.

Recovery from the Recovery Account for a real estate agent's fraud is limited to acts within the scope of the agent's license. *Davis v Harris* (1998) 61 CA4th 507, 71 CR2d 591.

Because the Recovery Account is intended to compensate innocent members of the public who are victimized by dishonest licensees, real estate licensees themselves are not within the class of persons entitled to compensation from the account. *Wallace v Onate* (1991) 2 CA4th 549, 3 CR2d 3.

NOTE: The Recovery Account must deny recovery for injuries inflicted by a salesperson unless the applicant also pursues recovery from the salesperson's broker. Thus, a Recovery Account applicant who holds a judgment against a salesperson, but not the salesperson's broker, will have to show that the salesperson was acting outside the scope of his or her employment or was not employed by a broker at the time of the disputed transaction. Bus & P C §10471(d).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.168 d. No Discharge in Bankruptcy

§2.168 d. No Discharge in Bankruptcy

The claimant must represent in its application that the underlying judgment and debt have not been discharged in bankruptcy or, if the debtor's bankruptcy is pending or is filed after the application is filed, that the judgment and debt have been declared nondischargeable. Bus & P C §10471(c)(7)(F). This requirement reduces the risk of collusive judgments obtained for the sole purpose of recovering from the Recovery Account, and puts the burden on the claimant to protect its judgment in the debtor's bankruptcy proceeding. *Zinneman v Bagnol* (2002) 104 CA4th 656, 128 CR2d 342.

© The Regents of the University of California

§2.169 2. Amounts Recoverable

The maximum recovery in causes of action is $20,000 for any one transaction and $100,000 for any one licensee, regardless of the number of fraudulent acts by one broker. Bus & P C §10474; *Dombalian v Fox* (1979) 88 CA3d 763, 152 CR 86. Proration may be required if valid claims exceed the maximum amount. Bus & P C §10474.5. Within these statutory limits, the claimant is entitled to recover the amount of the judgment that cannot be satisfied from the licensee's assets, including prejudgment and postjudgment interest and costs. *Antonio v Hempel* (1977) 71 CA3d 128, 139 CR 309; *Nordahl v Department of Real Estate* (1975) 48 CA3d 657, 121 CR 794.

A party defrauded as part of a scheme involving multiple licensees may be entitled to recovery from the account of any licensed judgment debtor. Bus & P C §10474(d). If multiple licensees are involved in a scheme to defraud, more licensees may be available from whom the plaintiffs can recover the $100,000 limit per licensee, but the involvement of more licensees does not increase the $20,000 limit per real estate transaction. See *Edmonds v Augustyn* (1987) 193 CA3d 1056, 238 CR 704 (scheme's subagents committed independent fraudulent acts that gave rise to individual liability and permitted victim to seek recovery from account of any licensed judgment debtor, not just from that of scheme's leader).

Only the applicants' direct losses are compensable. In, *e.g., Temple v Kerwin* (1989) 209 CA3d 1087, 257 CR 651, emotional distress, punitive damages, and costs were held not recoverable. Tax benefits are deducted from amounts claimed (*Froid v Fox* (1982) 132 CA3d 832, 183 CR 461), as are attorney fees and punitive damages (*Lewis v Edmonds* (1987) 190 CA3d 1101, 235 CR 835; *Acebo v Real Estate Educ., Research & Recovery Fund* (1984) 155 CA3d 907, 202 CR 518).

© The Regents of the University of California

§2.170 3. Procedures

A claimant with a proper judgment may apply to the DRE for an order directing payment of the claim from the Recovery Account. Application must be made within 1 year after the judgment becomes final, and the applicant must show that reasonable attempts were made to levy on the assets of "all judgment debtors and all other persons liable" to the applicant in the transaction or that the applicant has otherwise used reasonable diligence to pursue the available remedies. Bus & P C §10471(c)(7)(E). See *Mason v Department of Real Estate* (2002) 102 CA4th 1349, 126 CR2d 278. See also *Fine v Southern Cal. Bus. Sales* (1987) 190 CA3d 480, 235 CR 489.

For details on how the claimant must serve the judgment debtor, response time, the commissioner's rights and duties regarding the application, and the claimant's rights of de novo review upon denial, see Bus & P C §§10471.1-10472.

NOTE: If a federal court issued the underlying judgment, the application may be filed either in the superior court of any California county that would have been a proper venue of the underlying lawsuit or in the superior court of Sacramento County. Bus & P C §10472(a).

On payment from the fund, the license of the broker or salesperson is automatically suspended until the fund has been reimbursed with interest. Bus & P C §10475. The reimbursement obligation is not dischargeable in bankruptcy. 11 USC §523(a)(11).

This automatic suspension does not violate a real estate broker's due process rights. The required notice and opportunity to provide written argument satisfy due process requirements, and a full and formal hearing with oral testimony is not necessary. *Rodriguez v Department of Real Estate* (1996) 51 CA4th 1289, 59 CR2d 652. The licensee may obtain a judicial review of the suspension by petitioning the appropriate superior court for a writ of mandamus. Such petition must be filed within 30 days of receipt of notice of the Real Estate Commissioner's decision. Bus & P C §10471.5(c).

© The Regents of the University of California

VIII. DISCIPLINARY PROCEEDINGS

A. Real Estate Commissioner Proceedings

§2.171 1. Grounds for Imposing Discipline

Under the Real Estate Law (Bus & P C §§10000-10580), the Real Estate Commissioner has substantial authority to bring disciplinary proceedings against brokers and salespersons. Bus & P C §§10071, 10176-10177.

NOTE: Jurisdiction for enforcement of the Real Estate Law rests with the Commissioner. There is no private right of action created for a party to sue a broker for a violation of the Real Estate Law. See *Moradi-Shalal v Fireman's Fund Ins. Co.* (1988) 46 C3d 287, 294, 250 CR 116; *Vikco Ins. Servs., Inc. v Ohio Indemn. Co.* (1999) 70 CA4th 55, 62, 82 CR2d 442; *Grabau v Brown (In re Grabau)* (Bankr ND Cal 1993) 151 BR 227.

The grounds for disciplining licensees are broad; they include all breaches of fiduciary duty under general agency law. Bus & P C §§10176-10177; *Rhoades v Savage* (1963) 219 CA2d 294, 32 CR 885. Effective January 1, 2005, the statutory grounds for discipline include failure to disburse funds in accordance with a loan commitment and intentional delay in closing a loan for the purpose of increasing interest, fees, or other costs payable by the borrower. Bus & P C §10176(k)-(*l*). In addition, the Real Estate Law specifies several actions that may not be breaches of fiduciary duty under their particular circumstances but that nonetheless may subject the broker to license suspension or revocation. See Bus & P C §§10177-10177.4.

To the extent that regulatory goals would be furthered, licensees may even be disciplined for certain misconduct that is not directly related to their conduct as licensees. *Stickel v Harris* (1987) 196 CA3d 575, 589, 242 CR 88, quoting *Jennings v Karpe* (1974) 36 CA3d 709, 111 CR 776. For example, under Bus & P C §10177(f), the DRE can suspend or revoke a real estate license based on the suspension or revocation of a license issued by another government agency. See *Herrera v Department of Real Estate* (2001) 88 CA4th 776, 106 CR2d 232 (real estate license revoked after licensee was temporarily suspended from practice of law for misappropriating client's funds).

Conviction of a crime, however, alone cannot support either disciplinary action or denial or revocation of a license unless the crime is "substantially related to the qualifications, functions, or duties of the business or profession." Bus & P C §§480(a), 490. See *Brandt v Fox* (1979) 90 CA3d 737, 153 CR 683 (denial of license based on conviction for possession of controlled substance was not shown to be substantially related to the qualifications, functions, or duties of real estate licensee).

In *Chodur v Edmonds* (1985) 174 CA3d 565, 220 CR 80, the term "dishonest dealing," a ground for discipline under Bus & P C §10177(j), was held to be not unconstitutionally vague either on its face or as applied. The broker in *Chodur* had intentionally not made payments on an underlying note, although he received payments from his borrowers under his all-inclusive promissory note, and then used the payments received for his own benefit.

PRACTICE TIP: Claimants may obtain complaint forms from the DRE's website (the website is listed in the Directory). After a complaint is filed, the matter is first turned over to an investigator, who usually contacts the broker and advises the broker of the claim. Brokers and practitioners acting on behalf of the accused should use this investigation period and should respond to the complaint by explaining the conduct in question as completely as possible before an accusation is formally filed. Spurious or nonmeritorious claims can often be defeated in this manner. Claimants should recognize that if there is a pending civil action based on the acts under investigation, the DRE may choose to delay the investigation and/or resolution of the claim until after the legal action is resolved.

On disciplinary procedures, see California Real Estate Brokers: Law and Litigation, chap 9 (Cal CEB 2009).

© The Regents of the University of California

2. Procedures and Remedies

§2.172 a. Mitigating Factors

If the broker's activities violate the Real Estate Law (Bus & P C §§10000-10580), disciplinary proceedings may be instituted despite the licensee's good faith, the absence of damage, lack of an enforceable agreement to compensate the licensee, absence of gain to the licensee, or absence of any civil action against the licensee. *Buckley v Savage* (1960) 184 CA2d 18, 7 CR 328 (no pecuniary loss suffered); *Abell v Watson* (1957) 155 CA2d 158, 317 P2d 159 (absence of damage); *de St. Germain v Watson* (1950) 95 CA2d 862, 214 P2d 99 (licensee in good faith). In mitigating the penalty, however, Real Estate Commissioner may consider the absence of injury to the principal, advantage to the broker, or intent by the broker to act in a fraudulent or dishonest manner. 95 CA2d at 870.

© The Regents of the University of California

§2.173 b. Disciplinary Proceedings

Disciplinary proceedings for violating the Real Estate Law (Bus & P C §§10000-10580) are usually in the form of license suspensions or revocations under Bus & P C §10175. With limited exceptions (*e.g.,* fraudulent procurement of license; see Bus & P C §10177.1), the Real Estate Commissioner must hold a hearing before suspending or revoking a license. Bus & P C §10100. Hearings are conducted by an administrative law judge from the Office of Administrative Hearings in accordance with the Administrative Procedures Act (Govt C §§11500-11529). Govt C §11502. Limited discovery may be taken before the hearing. Govt C §§11507.5-11507.7, 11511.

NOTE: A broker charged in a disciplinary proceeding will not be able to obtain, in discovery, copies of audit or enforcement manuals that the DRE uses to enforce its own regulations; these publications are considered confidential and privileged material. *Suarez v Office of Admin. Hearings* (2004) 123 CA4th 1191, 20 CR3d 618. Thus, the broker must prove its case objectively, by and through existing case and statutory law and the evidence, and not by use of internal DRE regulatory documents.

Rules of evidence may be relaxed under standards governing administrative hearings. Govt C §11513. After the hearing, the hearing officer prepares a Proposed Decision containing the findings and, if applicable, a proposed penalty. Govt C §11517. The Real Estate Commissioner must then adopt the decision in its entirety, adopt the decision but reduce or mitigate the proposed penalty, or reject the proposed decision and penalty. Govt C §11517(c). If a disciplinary proceeding is pending, a real estate licensee may petition the Real Estate Commissioner to accept a voluntary surrender of his or her license. If accepted, relicensing occurs only if the Real Estate Commissioner grants a petition for reinstatement (Govt C §11522). Bus & P C §10100.2.

The procedure for reconsideration of the administrative decision is set forth in Govt C §11521(a). The decision may be judicially reviewed by means of administrative mandamus. Govt C §11523; CCP §1094.5. See California Administrative Mandamus (3d ed Cal CEB 2003). In reviewing the decision, the trial court exercises its independent judgment on whether the evidence supports the findings, and an appellate court will decide whether substantial evidence supports the trial court's findings. *Madrid v Department of Real Estate* (1984) 152 CA3d 454, 199 CR 520.

To commence a disciplinary proceeding, the Real Estate Commissioner must file an accusation under Govt C §11503 within 3 years from the occurrence of the alleged grounds for the disciplinary action. Bus & P C §10101. If the ground is fraud, misrepresentation, or a false promise, the accusation must be filed within the later of 1 year after the discovery by the aggrieved person of the grounds or 3 years after the occurrence of the grounds. Bus & P C §10101. If the actual misconduct of the licensee is the ground for the discipline, the limitations period begins with the misconduct. If the ground for the discipline is another official action, such as a criminal conviction, civil judgment, or the disciplinary action of another regulatory agency, the 3-year limitations period begins to run when the official action occurs, not on the date of the misconduct that resulted in the official action. See *Herrera v Department of Real Estate* (2001) 88 CA4th 776, 106 CR2d 232 (§10101 limitations period for real estate licensee suspended from practice of law ran from date of suspension of law license, not date of underlying misconduct); *California Real Estate Loans, Inc. v Wallace* (1993) 18 CA4th 1575, 23 CR2d 462 (3-year limitations period for discipline based on civil judgment for fraud, misrepresentation, or deceit runs from date of final judgment, not date of underlying acts or omissions).

© The Regents of the University of California

§2.174 c. Remedies

Most penalties involve some form of temporary license suspension or permanent revocation. Bus & P C §§10175-10176. The Real Estate Commissioner, however, is also empowered to bring a civil action for violations of the Real Estate Law (Bus & P C §§10000-10580) and to issue desist and refrain orders to anyone, including a licensee, who violates that law. Bus & P C §§10081, 10086. A corporation's real estate broker's license cannot be revoked for violation of the Real Estate Law if the violating broker had completely disassociated himself from the corporation at the time of revocation. See *Amvest Mortgage Corp. v Antt* (1997) 58 CA4th 1239, 68 CR2d 457. Clarifying legislation was passed, effective January 1, 1999, to provide that the DRE may still discipline the corporation or deny it a license, even if the violator has disassociated from the corporation, if the offending officer, director, or stockholder violated the Real Estate Law while acting on behalf of the corporate broker. See Bus & P C §10177. A licensee who receives a desist and refrain order is entitled to an administrative hearing on the order. If the licensee files a verified request for a hearing, alleging that the order precludes him or her from engaging in a substantial portion of the licensee's business, the Real Estate Commissioner must initiate a civil action to enforce the desist and refrain order. Bus & P C §10086.

The Real Estate Law also imposes criminal sanctions for various actions by real estate licensees, including willful violations of the law. Bus & P C §10185. The district attorney of the county in which the violation occurs has jurisdiction to prosecute such actions, and the Real Estate Commissioner may participate in those proceedings. Bus & P C §10130.

The Real Estate Commissioner is authorized under Bus & P C §10175.2 to impose or accept a monetary penalty instead of suspending a licensee's license. The amount may not exceed $250 for each day of suspension or $10,000 for each decision. The money is deposited in the Recovery Account of the Real Estate Fund. See discussion of the Recovery Account in §§2.164-2.170; on the relationship between the Recovery Account and the Real Estate Fund, see Bus & P C §10450.6.

© The Regents of the University of California

§2.175 B. Local Association of Realtors® Proceedings

As members of the California Association of Realtors® (CAR) and National Association of Realtors® (NAR), brokers and salespersons must conduct themselves according to the NAR Code of Ethics. Violation of the standards of conduct may result in suspension, expulsion, censure, or reprimand. In limited instances, fines may also be levied.

The NAR Code of Ethics also requires members to arbitrate with each other to the extent that the dispute arose from the real estate business. NAR Code of Ethics, art 17. Many local associations' bylaws also require arbitration of disputes with members of the general public. Such arbitration may provide a fast and inexpensive way to resolve some disputes. For local rules, counsel should refer to the bylaws of individual associations.

To obtain a copy of the Code of Ethics and Standards of Practice or the Interpretations of the Code of Ethics, call the National Association of Realtors® at the number given in the Directory.

The California Association of Realtors® also publishes the California Code of Ethics and Arbitration Manual. A copy of this manual can be purchased from CAR or a local association or board. See the Directory.

Multiple listing service (MLS) participants or subscribers who violate the MLS rules are subject to discipline. CAR publishes the Model MLS Rules that have been adopted by most of the local associations and boards, although attorneys should check for local variations.

© The Regents of the University of California

§2.176 IX. BROKER LIABILITY TO THIRD PARTIES

The broker owes no fiduciary duty to any person other than his or her principal, but the broker has a general duty under the Real Estate Law (Bus & P C §§10000-10580) to deal fairly and honestly with all parties to any real estate transaction. Bus & P C §10176(i). Brokers have been held liable to third parties under a number of theories discussed in §§2.177-2.182.

© The Regents of the University of California

§2.177 A. Secret Profits

A broker can be held liable to a third party for secret profits received through fraud or misrepresentation and can be compelled to disgorge those profits whether or not the third party suffered any actual loss. *Ward v Taggart* (1959) 51 C2d 736, 336 P2d 534.

The broker remains a fiduciary after becoming a principal in the transaction, even if the buyer-broker did not know at the time of purchase that a larger profit would be made by selling the property to a third party buyer. The "secret profit" still must be disgorged to the principal. *Roberts v Lomanto* (2003) 112 CA4th 1553, 5 CR3d 866. See §2.139 for discussion of a broker's liability to the principal for secret profits.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.178 B. Fraud, Misrepresentation, and Failure to Disclose

§2.178 B. Fraud, Misrepresentation, and Failure to Disclose

A broker's dealings with a third party to the transaction, to whom the broker owes no fiduciary responsibility, are generally measured by the same obligations that the principal owes to the third party, because the broker is the principal's agent. The broker has the same affirmative obligations as the seller to disclose material facts, and not to misrepresent them, whether negligently or intentionally. These obligations are founded in long-standing principles of common law. The obligation to disclose includes matters concerning the value or desirability of the property that the broker knows or reasonably should know. *Lingsch v Savage* (1963) 213 CA2d 729, 29 CR 201. On the seller's duty to disclose, see §§4.45, 5.6-5.29. These common law obligations of honesty and fair dealing apply in both commercial and residential transactions, but the residential broker will further need to comply with the statutory duties of disclosure set forth in CC §§2079-2079.11.

The identity of the persons receiving the disclosure and their status as parties in the transaction is pivotal in deciding whether the broker has a duty to disclose. The broker owes this duty only to a person or entity who is a *party* to the transaction. "Only a transferee, that is, the ultimate purchaser, can recover from a broker or agent for breach of these duties." *Coldwell Banker Residential Brokerage Co., Inc. v Superior Court* (2004) 117 CA4th 158, 165, 11 CR3d 564.

Whether a particular fact regarding the property is sufficiently material to require affirmative disclosure depends on the context of each case. *Saporta v Barbagelata* (1963) 220 CA2d 463, 33 CR 661. For example, the seller and the broker must disclose the following:

- Known termite and fungus infestation (*Saporta v Barbagelata, supra*);
- Improvements have been built on landfill (*Central Mut. Ins. Co. v Schmidt* (1957) 152 CA2d 671, 313 P2d 132);
- Improvements are not within property boundaries (*Walters v Marler* (1978) 83 CA3d 1, 147 CR 655); and
- The correct size of the property (*Cory v Villa Props.* (1986) 180 CA3d 592, 225 CR 628).

See also *Furla v Jon Douglas Co.* (1998) 65 CA4th 1069, 76 CR2d 911 (seller and listing agent who overestimated square footage of residence by more than 20 percent may be liable to buyer). But in *Blickman Turkus, LP v MF Downtown Sunnyvale, LLC* (2008) 162 CA4th 858, 877, 76 CR3d 325, the court found that a broker who represented the tenant in a complex commercial lease transaction *did not* have a duty to inform the landlord, after the lease was signed but before possession, about the tenant's deteriorating financial condition. The court noted that any financial information had been obtained by reason of the broker's fiduciary relationship with the tenant and that if the possession of such knowledge were enough to trigger a duty to disclose, it would be impossible for intermediaries such as brokers to act for their principals in business transactions. 162 CA4th at 877. See also *FSR Brokerage, Inc. v Superior Court* (1995) 35 CA4th 69, 41 CR2d 404 (broker who failed to disclose to buyer alleged defects in residential balcony that later collapsed, injuring and killing buyer's guests, had no duty to guests). Compare *FSR Brokerage* with *Geernaert v Mitchell* (1995) 31 CA4th 601, 37 CR2d 483, in which the buyers were able to state a cause of action against a predecessor of their seller for alleged misrepresentations.

The broker also has disclosure responsibilities mandated as statutory duties by various sections of the Real Estate Law (Bus & P C §§10000-10580) and regulations adopted by the Real Estate Commissioner. See §§2.131, 2.171.

If no disclosure is made, the broker and the seller are jointly and severally liable for the full amount of the buyer's damages. If a broker is aware of misrepresentations that the seller has made directly to the buyer, the broker is obligated to correct them; the broker has no duty to conceal fraudulent or dishonest acts of the principal. *Willig v Gold* (1946) 75 CA2d 809, 171 P2d 754. If the broker misrepresents a material fact to the buyer, the seller will be liable along with the broker under a respondeat superior theory. See §§2.184-2.187. Statutory duties applicable to a residential broker, however, do not relieve the buyer from exercising reasonable diligence to protect its own interests. CC §2079.5.

In *Manderville v PCG&S Group, Inc.* (2007) 146 CA4th 1486, 55 CR3d 59, the court was concerned with the effect that an express exculpatory clause in favor of the brokers would have on their affirmative misrepresentation that the residential lot could be split. The clause expressly advised buyers of their right to conduct inspections, including the

right to investigate matters affecting the value or desirability of the property, such as ordinances affecting future development and zoning of the property. The clause went on to strongly advise the buyer to investigate such conditions. In overruling the claim that the clause precluded justifiable reliance, the court noted that, as a matter of public policy, a contract cannot exempt anyone from responsibility for his or her fraud or willful injury to persons or property.

The statutes of limitation for actions by third parties against brokers correlate to the statutes of limitation for actions by a principal against the broker. The limitations period for actions concerning a residential real estate broker's breach of duty to disclose is 2 years under CC §2079.4, which applies to causes of action against brokers for negligent misrepresentation. *Loken v Century 21-Award Props.* (1995) 36 CA4th 263, 42 CR2d 683. This statute of limitations does not apply to causes of action for negligence or fraud (*Williams v Wells & Bennett Realtors* (1997) 52 CA4th 857, 61 CR2d 34) or breach of fiduciary duty (*Field v Century 21 Klowden-Forness Realty* (1998) 63 CA4th 18, 73 CR2d 784).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.179 C. Negligence

§2.179 C. Negligence

A broker who renders service in a negligent manner is generally liable to any third person within the zone of foreseeable risk who is injured by the negligent act. *Merrill v Buck* (1962) 58 C2d 552, 25 CR 456 (landlord's rental agent liable to tenant for failure to disclose dangerous condition); *Easton v Strassburger* (1984) 152 CA3d 90, 199 CR 383 (seller's listing agent liable to buyer for failure to disclose damaged property). Whether such duty is owed in a particular case is based on several factors, including the extent to which the transaction was intended to affect the plaintiff, the foreseeability of harm, the degree of certainty that the plaintiff suffered injury, the nexus between the defendant's conduct and the injury suffered, the moral blame attached to the defendant's conduct, and the policy of preventing future harm. *Merrill,* 58 C2d at 562. See *Blickman Turkus, LP v MF Downtown Sunnyvale, LLC* (2008) 162 CA4th 858, 891, 76 CR3d 325 (court refused to extend broker's "duty to deal honestly and fairly with all parties in a sales transaction" when plaintiff failed to allege that broker could have prevented foreseeable harm); *FSR Brokerage, Inc. v Superior Court* (1995) 35 CA4th 69, 41 CR2d 404 (when broker failed to disclose to buyer alleged defects in residential balcony that later collapsed, injuring and killing buyer's guests, court held the broker had no duty to guests). The broker will be held liable to third parties for the negligence of salespersons in his or her employ. Bus & P C §10177(h); CC §2343(3); *Merrill v Buck, supra*. *Easton v Strassburger, supra,* enunciated the residential listing broker's affirmative duty to conduct a reasonably competent and diligent inspection of the property listed for sale. This duty was later codified and included in a specific disclosure form to be signed by the seller and the brokers. CC §§1102-1102.17; see §§2.133-2.134.

© The Regents of the University of California

§2.180 D. Breach of Contract

Although third party breach of contract cases against brokers are less common than cases brought on tort theories, because a broker typically acts on behalf of a disclosed principal, the breach of contract theory is useful in certain instances. A broker may also be held liable to a third party for breach of an agreement that is ancillary to the contract to convey. In *Barr v Rhoades* (1969) 274 CA2d 852, 79 CR 505, the sellers and their brokers were held liable for damages when they breached their agreement with the buyer to secure tenants and financing in connection with the sale of an apartment building.

An agent who knowingly enters into a contract without the authority to do so becomes liable as a principal. CC §2343(2).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/2 Brokers/§2.181 E. Housing Discrimination

§2.181 E. Housing Discrimination

Brokers who participate in discriminatory practices in the housing market may incur liability under any of a number of fair housing statutes. Brokers have been held to be covered by California's Unruh Civil Rights Act (CC §51) (*Lee v O'Hara* (1962) 57 C2d 476, 20 CR 617; *Vargas v Hampson* (1962) 57 C2d 479, 20 CR 618), and the fact that a broker was merely following instructions from the principal is not a defense to an Unruh Civil Rights Act suit (*Wagnerv O'Bannon* (1969) 274 CA2d 121, 79 CR 44). An association of Realtors® or a multiple listing service might also incur liability under the Unruh Civil Rights Act if it accedes to a seller's wish to market property in a discriminatory manner. *Wagner v O'Bannon, supra*. Furthermore, to deny access to, membership in, or participation in a multiple listing service or other real estate brokerage association or service because of race, color, religion, sex, sexual orientation, marital status, ancestry, disability, familial status, source of income, or national origin is prohibited by Govt C §12955(j). "Religion" includes all aspects of religious belief, observance, and practice. CC §51(e)(3). These enumerated factors include a perception that the person has any particular characteristic within the listed categories or that the person is associated with a person who has, or is perceived to have, any particular characteristic within the listed categories. CC §51(e)(5).

The Fair Housing Act (FHA) (42 USC §§3601-3631; commonly referred to as Title VIII of the Civil Rights Act of 1968) and the Civil Rights Act of 1866 (42 USC §§1981-1982) prohibit discriminatory practices in the sale or rental of a dwelling and serve as potential bases for imposing liability for damages on brokers who participate in discriminatory practices. The FHA applies to selling, renting, making loans secured by residential property, making appraisals, enforcing age discrimination covenants in common interest developments, and advertising residential properties. See 42 USC §§3604-3605; 24 CFR §§100.50(b), 100.75. The FHA covers discrimination by race, color, sex, national origin, religion, familial status, and disability, with exemptions for the following types of housing:

- Single-family homes for sale or rent by the owner, if specified conditions are met (42 USC §3603(b)(1));
- Most rentals by religious organizations and clubs (42 USC §3607(a));
- Housing with reasonable local, state, or federal restrictions on the maximum number of occupants (42 USC §3607(b)(1)); and
- Qualified housing for seniors (42 USC §3607(b)(1)-(3)).

The Supreme Court unanimously held that an individual who was a real estate company's president and sole shareholder was not vicariously liable for violations of the FHA committed by a salesperson employed by the company. *Meyer v Holley* (2003) 537 US 280, 154 L Ed 2d 753, 123 S Ct 824. Rather, under traditional agency principles, the real estate corporation, not its owner or officer, was the deemed principal or employer and thus subject to vicarious liability for torts committed by its agents or employees. In the absence of a clear congressional intent to expand the common law principles of vicarious liability, neither the right of an officer or shareholder to control the salesperson, nor the overriding societal priority of the FHA's objectives, warranted extending tort-related vicarious liability rules to include the officer and shareholder. Furthermore, the Court found no support under the FHA itself for imposing a nondelegable duty on officers or shareholders to ensure that a corporation's salespersons do not discriminate.

Private actions alleging that brokers engaged in the practice of steering African Americans into, and Caucasians out of, certain neighborhoods were upheld in *Gladstone, Realtors v Bellwood* (1979) 441 US 91, 60 L Ed 2d 66, 99 S Ct 1601, and *Broadmoor Improvement Ass'n v Stan Weber & Assocs.* (5th Cir 1979) 597 F2d 568.

Another possible basis for imposing liability on brokers for discriminatory practices is the California Fair Employment and Housing Act (Govt C §§12900-12996). Under Govt C §12920, the "practice of discrimination because of race, color, religion, sex, marital status, national origin, ancestry, familial status, disability or sexual orientation in housing accommodations is declared to be against public policy." Moreover, the "opportunity to seek, obtain, and hold housing without discrimination" by members of these protected classes was declared to be a civil right. Govt C §12921(b).

A broker who supplies information on the race, color, sex, religion, ancestry, or national origin of a prospective buyer, even when requested by the seller, violates the California Fair Employment and Housing Act (FEHA) (Govt C §§12900-12996). 53 Ops Cal Atty Gen 196 (1970). In *Smith v Fair Employment & Hous. Comm'n* (1996) 12 C4th 1143,

51 CR2d 700, the supreme court held that the free exercise clauses (guaranteeing freedom of religion) of the federal and state constitutions could not be relied on by a landlord who refused to rent an apartment to an unmarried couple and thereby discriminated against them on the basis of their marital status in violation of Govt C §§12948, 12955(a), (d), and CC §51.

In *Thomas v Anchorage Equal Rights Comm'n* (9th Cir 2000) 220 F3d 1134, the Ninth Circuit heard a challenge to an Alaska antidiscrimination housing law (similar to California's) brought by Christian landlords who refused to rent to unmarried couples on religious grounds. After first finding for the landlords (see *Thomas v Anchorage Equal Rights Comm'n* (9th Cir 1999) 165 F3d 692) and creating a religious exception to the antidiscrimination law, the court, sitting en banc, vacated the decision, finding that even if prosecution under the statute was theoretically possible, it was not reasonable or imminent (citing the lack of enforcement) and therefore failed the constitutional requirement of ripeness.

Brokers are also subject to administrative action under the Real Estate Law (Bus & P C §§10000-10580) to revoke the broker's license. Bus & P C §10177(l); 10 Cal Code Regs §§2780-2781. See also Bus & P C §§125.6, 10170.5(a)(4); 10 Cal Code Regs §2725. See discussion of disciplinary actions in §§2.171-2.175. A tort cause of action may also be available.

For a detailed discussion of federal antidiscrimination laws, see California Landlord-Tenant Practice §§2.29-2.47 (2d ed Cal CEB 1997); for a detailed discussion of California antidiscrimination and fair housing laws, see Landlord-Tenant §§2.48-2.60.

© The Regents of the University of California

§2.182 F. Anti-Money-Laundering Laws

Brokers and attorneys involved in real estate closings may be required to establish anti-money-laundering programs under federal law. Section 352(a) of the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (USA PATRIOT Act) (Pub L 107-56, 115 Stat 272) amended the Bank Secrecy Act (31 USC §§5311-5330) to require every financial institution to establish such programs. 31 USC §5318(h). The Bank Secrecy Act defines "financial institution" to include "persons involved in real estate closings and settlements." 31 USC §5312(a)(2)(U). On April 29, 2002, and on November 6, 2002, the Secretary of the Treasury temporarily exempted such persons from the requirement to establish anti-money-laundering programs. 31 CFR §103.170(b)(1)(vi); 67 Fed Regs 21110 and 67547 (2002). The Financial Crimes Enforcement Network, acting under a delegation of authority from the Secretary of the Treasury, has published a notice of proposed rule-making to solicit public comments on whether "persons involved in real estate closings and settlements" pose a significant money-laundering risk and whether such persons should be permanently exempted. 68 Fed Reg 17569 (2003). The deadline for comments was June 9, 2003. When the 2007 edition of this book went to press, the temporary exemption remained in effect and the Secretary of the Treasury had not published a rule on the issue.

If the Secretary of the Treasury ultimately determines that they are subject to the anti-money-laundering requirements, real estate brokers and attorneys will be required to establish programs that include the development of internal policies, procedures, and controls; the designation of a compliance officer; an ongoing employee-training program; and an independent audit procedure to test the programs. 31 USC §5318(h)(1). The Secretary may impose a civil penalty of up to $100,000 for a willful violation and up to $50,000 for a pattern of negligent violations of the requirements. 31 USC §5321(a)(1), (6). In addition, a willful violation is punishable by a criminal penalty of up to $250,000 and 5 years in prison. 31 USC §5322(a).

© The Regents of the University of California

§2.183 G. Principal to Broker; Indemnification

The broker's duty to disclose property defects is coextensive with the seller's (see §2.178). *Lingsch v Savage* (1963) 213 CA2d 729, 29 CR 201. Generally, the broker and the seller will be jointly and severally liable for the broker's misrepresentations to a buyer. *Saporta v Barbagelata* (1963) 220 CA2d 463, 33 CR 661. If a broker merely relays a misrepresentation from the seller to the buyer and is unaware of its falsity, the broker may escape liability for fraud but may still be liable for negligence, although the basis of the seller's liability would be fraud. *Gardner v Murphy* (1975) 54 CA3d 164, 126 CR 302. In this situation, the broker may be entitled to full indemnification from the principal for any liability incurred. *Gardner v Murphy, supra*.

The law of equitable indemnity has been adopted into broker-principal situations. In *Easton v Strassburger* (1984) 152 CA3d 90, 199 CR 383, the court looked for guidance to the leading case in the indemnity area, *American Motorcycle Ass'n v Superior Court* (1978) 20 C3d 578, 146 CR 182. The *Easton* court recognized that while full, pre-*American Motorcycle* indemnification might be appropriate when culpability was heavily weighted in one direction, that case had modified the equitable indemnity doctrine to permit sharing among co-tortfeasors, based on fault. Thus, the former "active-passive" distinction no longer applied. See also *Far W. Fin. Corp. v D & S Co.* (1988) 46 C3d 796, 251 CR 202, restating the rule of *American Motorcycle*.

NOTE: The listing agreement may provide for contractual indemnity, which is an entirely different basis for indemnification. The California Association of Realtors® Residential Listing Agreement (Exclusive Authorization and Right to Sell), for example, contains a clause in which the principal agrees to hold the broker harmless for liability incurred when the principal supplies incorrect information or fails to disclose a material fact. See §2.57.

The 2-year statute of limitations for actions concerning a real estate broker's breach of duty to disclose does not apply to an implied contractual indemnity action between sellers and their broker. *West v Superior Court* (1994) 27 CA4th 1625, 34 CR2d 409.

© The Regents of the University of California

X. PRINCIPAL LIABLE TO THIRD PARTIES FOR BROKER'S ACTS

§2.184 A. Misrepresentations and Nondisclosure

Under general rules of agency law, a principal is liable to third parties for the agent's actions undertaken on the principal's behalf, whether or not the principal was aware of or authorized the agent's actions. CC §2338; *Warshauer v Bauer Constr. Co.* (1960) 179 CA2d 44, 3 CR 570. In real property transactions, this rule makes the principal liable for the broker's misrepresentations whether the principal has knowledge of the misrepresentation (*Burkett v J.A. Thompson & Son* (1957) 150 CA2d 523, 310 P2d 56) or is innocent of it (*Miller v Wood* (1961) 188 CA2d 711, 10 CR 770). The principal is held liable for the broker's misrepresentations even when the broker is acting as the disclosed agent for both parties to the transaction. *Owens v Schneider* (1938) 29 CA2d 593, 85 P2d 198.

The broker's negligent, as well as intentional, misrepresentations will subject the principal to liability, whether or not the principal knew of or consented to the statements. CC §2338. Thus, the principal may incur liability if the broker should have known that the broker's statement was false but had no actual knowledge of its falsity. *Richard v Baker* (1956) 141 CA2d 857, 297 P2d 674. See also *Gagne v Bertran* (1954) 43 C2d 481, 275 P2d 15.

NOTE: "As against a principal, both principal and agent are deemed to have notice of whatever either has notice of, and ought, in good faith and the exercise of ordinary care and diligence, to communicate to the other." CC §2332. This section allows recovery against a principal based upon the knowledge of the agent.

Both the broker and the seller have an affirmative obligation to disclose property defects that would not be apparent to a buyer (see §2.178). *Lingsch v Savage* (1963) 213 CA2d 729, 29 CR 201. Because the broker's knowledge is imputed to the seller, a seller without actual knowledge of a defective condition is liable if the broker knows of the defects and fails to disclose them. *Rothstein v Janss Inv. Corp.* (1941) 45 CA2d 64, 113 P2d 465; CC §§2333, 2338. The broker's knowledge is not imputed to the seller if the broker is acting in a dual capacity and thus has an interest adverse to that of the seller. *Herdan v Hanson* (1920) 182 C 538, 189 P 440; *Owens v Schneider, supra*. However, if a dual agent's fraud benefits one principal, the principal so benefited will be liable to the other. CC §2230. When a broker in a dual agency relationship finds that he or she has a conflict of interest related to a duty of disclosure, it may be incumbent on the broker to withdraw from the transaction rather than benefit one client over the other.

On principal's duties to brokers, see California Real Estate Brokers: Law and Litigation, chaps 5, 7 (Cal CEB 2009).

© The Regents of the University of California

§2.185 B. Effect of Exculpatory "As Is" Provision

Despite a common misperception, an "as is" or similar exculpatory provision in a purchase agreement will *not* immunize a seller from liability for failure to disclose known, hidden defects (*Lingsch v Savage* (1963) 213 CA2d 729, 29 CR 201; see *Shapiro v Hu* (1986) 188 CA3d 324, 233 CR 470; *Katz v Department of Real Estate* (1979) 96 CA3d 895, 158 CR 766), or from liability for the broker's fraudulent acts of which the seller has knowledge (*Herzog v Capital Co.* (1945) 27 C2d 349, 164 P2d 8; *Lingsch v Savage, supra*). Similarly, an "as is" sale does not shield an agent from liability, although the agent is not liable for foundation defects discoverable only by extraordinary efforts beyond the diligent inspection standard. *Wilson v Century 21 Great W. Realty* (1993) 15 CA4th 298, 18 CR2d 779. An innocent principal, however, is protected by an exculpatory provision from liability for damages for the agent's affirmative acts of misconduct. The injured party's only remedy is rescission. *Speck v Wylie* (1934) 1 C2d 625, 36 P2d 618.

An unanswered question is whether an exculpatory provision will protect an innocent principal from liability for damages for the broker's failure to disclose defects. See *Lingsch v Savage, supra*. Because the broker's knowledge of defects is imputed to the principal (see §2.184), and because an exculpatory clause will not protect a seller who knowingly fails to disclose defects, it could be argued that the rule of *Speck v Wylie, supra,* is limited to misrepresentations and would not apply to the broker's nondisclosure of defects. See *Herzog v Capital Co., supra*.

© The Regents of the University of California

§2.186 C. Broker's Failure to Disclose Principal

When a principal has authorized an agent to execute a contract on his or her behalf but the principal is not identified, the agent is personally liable on the contract. *Wedge v Security First Nat'l Bank* (1933) 219 C 113, 25 P2d 411. If the act is within the course and scope of the agency, the undisclosed principal is also liable. *Hulsman v Freland* (1928) 205 C 345, 270 P 948. The plaintiff, however, cannot hold both the principal and the agent liable. *Wedge v Security First Nat'l Bank, supra*. The plaintiff can be forced to decide whether to obtain a judgment against the agent or against the principal. 3 Witkin, Summary of California Law, *Agency and Employment* §160 (10th ed 2005).

© The Regents of the University of California

§2.187 D. Liability to Subsequent Purchasers

The seller's liability to third persons for the fraudulent misconduct of the seller or the seller's agent may extend to subsequent purchasers of the property. If the original buyer has a legally enforceable claim for damages for fraud by the seller or the seller's broker, a person who acquires the property from the original buyer can enforce the claim against the seller. *Burkett v J.A. Thompson & Son* (1957) 150 CA2d 523, 310 P2d 56. See also *Shapiro v Sutherland* (1998) 64 CA4th 1534, 76 CR2d 101 (subsequent buyer may bring action for fraudulent misrepresentation and material nondisclosure against former property owner who had sold to relocation company); *Geernaert v Mitchell* (1995) 31 CA4th 601, 37 CR2d 483 (subsequent buyers can sue former owners for fraudulent misrepresentation and concealment). Apparently, the original buyer must assign the claim to the subsequent buyer in order for the subsequent buyer to recover. *Cohen v Citizens Nat'l Trust & Sav. Bank* (1956) 143 CA2d 480, 300 P2d 14. But see *Varwig v Anderson-Behel Porsche/Audi, Inc.* (1977) 74 CA3d 578, 141 CR 539 (dealer who sold cars wholesale to another dealer can be liable to ultimate purchaser for misrepresentation of title).

The holding in *Cohen* that a subsequent purchaser, after learning that the builder had failed to disclose building code violations to the original buyer, could not sue the builder without an assignment of the cause of action from the original buyer, was criticized as "an unacceptably broad limitation of liability" in *Barnhouse v City of Pinole* (1982) 133 CA3d 171, 183 CR 881. The court in *Barnhouse* allowed a subsequent buyer to bring a direct action against the builder for failure to disclose underground seeps, springs, and slides to the original purchaser.

© The Regents of the University of California

3

Letters of Intent

Jamie O. Harris
Steve Stwora-Hail

I. WHAT IS A LETTER OF INTENT? §3.1

II. WHEN ARE LETTERS OF INTENT USED IN REAL PROPERTY SALES TRANSACTIONS? §3.2
- A. When Parties Prepare Letter Without Attorney's Assistance §3.3
- B. When Attorney Prepares Letter §3.4
  - 1. Factors to Consider in Using Letter of Intent §3.5
    - a. Time, Cost, and Efficiency §3.6
    - b. Method of Structuring the Transaction §3.7
    - c. Identification of "Deal-Breaker" Issues §3.8
    - d. Effect on Negotiations §3.9
    - e. Reduction of Risks Inherent in Partial Performance §3.10
    - f. Creation of Legally Binding Agreement on Certain Matters; Due Diligence and Confidentiality §3.11
    - g. Providing a Liquidated Damages Provision in a Letter of Intent §3.12
  - 2. When to Use Binding or Nonbinding Letter of Intent §3.13

III. RISKS OF USING A LETTER OF INTENT: WHEN IS IT BINDING? §3.14
- A. Unintended Enforceability of Letter of Intent §3.15
  - 1. Objective Manifestation of Mutual Assent §3.16
  - 2. How to Determine Intent §3.17
    - a. Parties' Conduct §3.18
    - b. Execution of Formal Documents Expressly Contemplated §3.19
    - c. Language Choice and Verb Tense §3.20
    - d. Specificity of Essential Terms §3.21
    - e. Conditional Third Party Approvals §3.22
    - f. Complexity and Size of Transaction §3.23
  - 3. Unexpected Enforceability in *Texaco v Pennzoil* §3.24
  - 4. Statute of Frauds §3.25
- B. Promissory Estoppel §3.26

IV. DUTY TO NEGOTIATE IN GOOD FAITH
- A. Basis for Existence of Duty §3.27
- B. Necessity of a Contract §3.28
- C. Recovery Limited to Reliance Damages §3.29
- D. Scope of Duty to Negotiate in Good Faith §3.30

V. NEGOTIATING AND DRAFTING A LETTER OF INTENT
- A. Negotiating and Drafting Considerations §3.31
- B. Letter of Intent §3.32
  - 1. Form: Letter Heading §3.33
  - 2. Form: Introductory Clause §3.34
  - 3. Form: Parties' Intentions on Binding or Nonbinding Nature of Letter §3.35
  - 4. Form: Description of Property §3.36
  - 5. Form: Purchase Price and Payment of Purchase Price §3.37
  - 6. Form: Deposits §3.38
  - 7. Form: Purchase and Sale Agreement §3.39
  - 8. Form: Buyer's Contingencies §3.40
  - 9. Form: Early Access for Inspections §3.41
  - 10. Form: Seller's Representations and Warranties §3.42
  - 11. Form: Escrow §3.43
  - 12. Form: Commissions §3.44
  - 13. Form: Confidentiality §3.45
  - 14. Form: Execution of Letter of Intent §3.46

© The Regents of the University of California

§3.1 I. WHAT IS A LETTER OF INTENT?

A letter of intent is a writing in which the parties to a proposed transaction state a mutual interest in or commitment to one or more important terms of an agreement and, in most cases, show a mutual intention to prepare a more definitive contract to embody the complete agreement.

A letter of intent may take a variety of forms, *e.g.,* a commitment letter, a memorandum of agreement, or an agreement in principle. The document may be a formal writing or an informal letter. The letter of intent may be legally binding in whole or in part, or it may be legally nonbinding. In real estate sales transactions, letters of intent are usually intended to be nonbinding.

The distinguishing characteristic of a letter of intent is that it does not and is not intended to contain all the terms and conditions contemplated by the parties to be part of a final complete contract for the deal. Rather, it is intended to contain only the important business and financial terms.

Although the parties may not intend the business terms contained in a letter of intent to be binding, by using a written letter of intent the parties may implicitly agree to negotiate in good faith. See §§3.27-3.30. By failing to negotiate in good faith a party may be subject to reliance damages suffered by the other party. See §3.29. The parties may specifically provide in the letter of intent that there is no obligation to negotiate in good faith, but such a provision may have a chilling effect on the continuing negotiations.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/3 Letters of Intent/§3.2 II. WHEN ARE LETTERS OF INTENT USED IN REAL PROPERTY SALES TRANSACTIONS?

§3.2 II. WHEN ARE LETTERS OF INTENT USED IN REAL PROPERTY SALES TRANSACTIONS?

Practice regarding letters of intent in real estate sales transactions varies considerably. Typically, the decision to use a letter of intent is made by the parties and their brokers. When a letter of intent is used in a real estate sale transaction, its purpose is usually to obtain preliminary written confirmation of the important points in the deal before the parties incur the time and expense of negotiating the details of the transaction and preparing definitive contract documents. In large or complex real estate transactions it is extremely cumbersome and expensive to negotiate basic terms of the deal through the exchange of full-length, detailed contract offers and counteroffers.

Letters of intent can serve the useful purpose of identifying and memorializing the parties' understanding on key points so that further negotiations on contract documents are limited to details. Letters of intent also permit the business participants to address controversial issues during the initial stages of a transaction when both sides are motivated to reach an agreement, before legal counsel begin negotiations. Letters of intent are almost never prepared in single-family residential transactions because residential brokers commonly use standard form purchase agreements such as California Association of Realtors® forms. See §6.3.

Some attorneys frequently use, or at least recommend, letters of intent because they can streamline the negotiation process. Others avoid using letters of intent if the transaction is relatively straightforward and it is more efficient to commence drafting a purchase and sale agreement. Because there does not appear to be a standard practice, the decision of whether to use a letter of intent in a particular transaction is a matter of professional judgment.

PRACTICE TIP: Counsel should consider using a letter of intent in the following situations:

- The transaction is complex;
- Counsel anticipates that the principal terms of the transaction will be aggressively negotiated by the other side; or
- It would be helpful to address certain issues before drafting a definitive statement.

© The Regents of the University of California

§3.3 A. When Parties Prepare Letter Without Attorney's Assistance

Attorneys are often confronted with a signed letter of intent prepared by the parties without an attorney's assistance. Although sophisticated parties may draft a problem-free letter of intent, any letter of intent can create significant problems if (1) it is unclear, (2) it fails to address one or more major transactional issues, or (3) the parties commence partial performance of the contract before executing a definitive contract.

These problems may be exacerbated if one party asserts that the letter of intent is a binding contract and the other asserts that it is merely a nonbinding statement of intent (see §§3.14-3.26). Because the term "letter of intent" means different things to different people, the parties may honestly disagree on whether they intended to create a binding or nonbinding letter of intent. However, given that the courts have recognized the ability of parties to enter into agreements to negotiate (see §3.27), it may be more difficult to enforce a binding letter of intent without either definitive language in the letter or unequivocal actions showing the parties' intent to be bound by the letter's terms.

PRACTICE TIP: An attorney presented with a signed letter of intent must first ascertain the client's goals. Does the client want to have a definitive contract prepared, the letter of intent enforced, or the letter of intent defended against another party's claim that a binding contract exists? The attorney must ascertain the client's intent and whether either party has begun performance or changed position in reliance on the letter of intent. Unless the client considers the letter of intent to be binding or the attorney forms the opinion that the letter is binding and that it is in the client's best interest to perform, the attorney should advise the client not to take any steps to perform the proposed contract until it is properly documented in a complete, signed agreement. On risks inherent in partial performance, see §§3.10, 3.14-3.26.

© The Regents of the University of California

§3.4 B. When Attorney Prepares Letter

As noted in §3.2, practice regarding letters of intent varies considerably, but many parties find them to be an effective tool. Letters of intent may be used in the following ways:

- By either party, as a preliminary negotiating tool with the expectation that the letter of intent will not be an enforceable contract, but merely a guide to further negotiation and contract drafting.
- By a prospective buyer—particularly if multiple buyers are competing for a desirable property—as a binding document, either as a commitment for the purchase and sale on the terms stated in the letter of intent, or as a commitment to exclusive negotiation for a period of time.
- As a cost-effective means of identifying potential "deal-breaking" issues and attempting to resolve them in a nonbinding understanding before time and money are spent on preparation of a detailed contract.

PRACTICE TIP: When drafting or reviewing letters of intent, the practitioner should keep in mind the risks and uncertainties involved in using such documents. The principal risk is the possibility of inadvertently creating a binding contract when the client desires only a nonbinding statement of intent for negotiating purposes. On binding and nonbinding letters of intent, see §§3.14-3.26.

On identifying the client's needs and objectives, see also §§1.23-1.57.

© The Regents of the University of California

§3.5 1. Factors to Consider in Using Letter of Intent

In determining whether to recommend that the client use a letter of intent and whether that letter of intent should be binding, the attorney should analyze the following factors:

- The time, cost, and efficiency of negotiating and drafting a letter of intent as compared with drafting a definitive agreement first (see §3.6);
- The structure provided by a letter of intent to guide the client through a complex sales transaction (see §3.7);
- The identification of potential "deal breakers" during the negotiation of a letter of intent, which may save time and money if they are discovered early (see §3.8);
- Streamlining negotiations by focusing the parties' attention on key transactional business issues before dealing with legal drafting details (see §3.9);
- A letter of intent's reduction of the risks inherent in partial performance (see §3.10); and
- The need for a legally binding agreement on certain matters (*e.g.,* confidentiality) before all terms and conditions are agreed on (see §3.11).

© The Regents of the University of California

§3.6 a. Time, Cost, and Efficiency

The attorney must evaluate competing time, cost, and efficiency considerations to ascertain whether negotiating and drafting a letter of intent will be more cost-effective than immediately negotiating and drafting a definitive purchase and sale agreement. If the strategic benefits of using a letter of intent outweigh its drawbacks, the attorney should consider recommending that a letter be drafted.

On the one hand, a letter of intent can be a cost-effective means of evaluating the parties' intent and identifying potential impasses at an early stage. On the other hand, preparing a detailed letter of intent means creating two separate negotiating and drafting projects: the letter of intent and the definitive agreement. The delay in drafting and negotiating the definitive agreement may postpone identification of important unanticipated issues that will appear only when the parties begin to document the details of that agreement.

PRACTICE TIP: The time, cost, and efficiency considerations are closely related to the size and complexity of the transaction. A straightforward sale of a modestly priced property may not justify use of a letter of intent, whereas a complex multi-million-dollar transaction may be more economical to document with a letter of intent as a contract drafting guide.

For further discussion of negotiating and drafting considerations, see §3.31.

© The Regents of the University of California

§3.7 b. Method of Structuring the Transaction

In complex transactions, a letter of intent can establish the scope of the various parties' responsibilities and the timing and sequence of events. It provides a useful scheme for structuring the transaction through negotiation of a definitive purchase and sale agreement to the closing and postclosing relations.

If one party uses more than one person to negotiate and complete the transaction, the letter of intent can help guide and limit later negotiations. The letter serves as a reminder of the preliminary understanding when persons not involved in the original negotiations attempt to make material changes in the deal.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/3 Letters of Intent/§3.8 c. Identification of 'Deal-Breaker' Issues

§3.8 c. Identification of "Deal-Breaker" Issues

A letter of intent can catalog the issues agreed to by the parties and identify issues that need further negotiation. By recognizing their mutual points of agreement, the parties can concentrate during negotiation on potential "deal breakers" and avoid spending time on noncontroversial topics. Even more important, the parties to the transaction are usually more amenable to compromise on "deal-breaker" issues at this stage of the negotiation.

© The Regents of the University of California

§3.9 d. Effect on Negotiations

Because a letter of intent is often written in everyday business language and targets key issues, it usually receives less scrutiny by the business principals than does a definitive written purchase and sale agreement. Attorneys are often not directly involved in negotiations at this stage but are assisting their clients behind the scenes. For the business person, the relatively easy-to-understand letter of intent can be an important tool for monitoring and controlling negotiation of the definitive purchase and sale agreement.

© The Regents of the University of California

§3.10 e. Reduction of Risks Inherent in Partial Performance

An attorney's recurring nightmare is a transaction in which the parties begin performance before they execute a definitive agreement. Many litigated letter of intent cases arise from partial performance of a contract in which only some of the terms are reduced to writing in the letter. See, *e.g., California Food Serv. Corp. v Great Am. Ins. Co.* (1982) 130 CA3d 892, 182 CR 67, discussed in §3.16. If there is partial performance, a party may be able to use a waiver or estoppel theory to render an original nonbinding letter of intent binding. See §§3.14-3.26.

If partial performance occurs, a well-drafted letter of intent can help to

- eliminate litigation by expressly stating that partial performance does not create a contract (see §§3.14, 3.26);
- clarify or protect the parties' rights and duties pending execution of the definitive purchase and sale agreement;
- reduce the risk of surprise when the agreement is completed;
- provide evidence of the contemplated provisions if the definitive agreement is never completed and problems arise; and
- limit damages to liquidated damages agreed to by the parties, rather than imposing specific performance (see §3.12).

EXAMPLE: The buyer may take any number of steps before executing a final purchase and sale agreement—many with the seller's knowledge, including lining up financing, hiring contractors, and commencing due diligence. The attorney should caution buyers about the risks of undertaking such steps before a definite agreement is signed. If the letter of intent will be nonbinding, it should specifically state that partial performance does not create a contract. For sample language for the letter of intent, see form 3.35-1.

© The Regents of the University of California

§3.11 f. Creation of Legally Binding Agreement on Certain Matters; Due Diligence and Confidentiality

A letter of intent can express a general nonbinding intent to engage in a particular sales transaction, while simultaneously creating specific legally binding agreements as conditions to moving forward with the intended purchase and sale. In a real estate sale, any legally binding portions of a letter of intent typically relate to such matters as access to information, obligations of confidentiality, and agreements not to solicit competing offers. Sometimes there is also an affirmative obligation to negotiate in good faith regarding the definitive agreement, though such an obligation may be implied by law (see §§3.27-3.30).

The letter of intent may allow a buyer the freedom to do a preliminary due diligence investigation, impose indemnification and insurance requirements on the buyer for claims arising from such an investigation, and allow a buyer to terminate further negotiations without liability if the investigation is not satisfactory. For example, a proposed buyer may obtain a limited time in which to conduct an environmental audit of real property. The attorney should, however, carefully consider the possible disadvantages of this approach.

For instance, the seller may find it disadvantageous because, to protect against closing claims, the seller may prefer that any due diligence investigation begin after execution of a definitive agreement. This approach allows the seller to retain control of disclosure by making it in an organized and well-documented manner. The seller may be reluctant to reveal any adverse information about a property on an informal basis under a letter of intent because a buyer who has not executed a definitive contract is generally less willing to accept adverse conditions than one who is committed to a deal. A seller may also wish to avoid disturbing tenants until a binding contract is signed.

The buyer may be unwilling to incur the potentially substantial cost of a due diligence analysis (*e.g.*, environmental studies, engineer's or architect's inspections, analysis of leases) until the property is "tied up" by a binding contract. On environmental investigations generally, see §§7.36-7.44.

PRACTICE TIP: The parties should consider including a binding confidentiality clause in the letter of intent. Some attorneys use a separate confidentiality agreement to better protect sensitive information that might be disclosed if all or part of the letter of intent protecting confidentiality is found to be nonbinding. See form 3.45-1.

© The Regents of the University of California

§3.12 g. Providing a Liquidated Damages Provision in a Letter of Intent

Parties generally intend for the deal terms listed in their letter of intent to be nonbinding. Sometimes letters of intent can unintentionally be deemed binding (see §§3.14-3.29). For these reasons, an attorney should consider inserting a liquidated damages provision in the letter of intent (see form 3.35-5). There has been no reported case in California that addresses the applicability of a liquidated damages provision in a letter of intent. Nevertheless, it would seem that if a court deemed binding a letter of intent that was otherwise sufficiently drafted to be nonbinding, but the parties' subsequent actions gave the court enough reason to find it binding, the court should also find the liquidated damages provision binding.

If the parties do not intend for the letter of intent to be binding, they should not object to including a liquidated damages provision in the letter of intent. Also, because the letter of intent is not intended to be binding, the parties should not have any expectation of damages if there is no transfer of the property. Therefore, a liquidated damages provision of a nominal sum (such as $100) should be considered an adequate amount, and far less than any party would otherwise need to expend defending a claim by the other party that the letter of intent was intended to be binding. If there are certain provisions within the letter of intent that the parties do intend to be binding, such as confidentiality or indemnification provisions (see §3.11), then the liquidated damages provision can be crafted to exempt specific obligations from the liquidated damages clause. Because no case law exists that addresses the applicability of a liquidated damages provision to a letter of intent, the practitioner is advised to satisfy the provisions of CC §§1671-1681 (dealing with the validity of liquidated damages in real property purchase contracts) as those statutes are applicable to a letter of intent. See form 3.35-5.

© The Regents of the University of California

§3.13 2. When to Use Binding or Nonbinding Letter of Intent

It is difficult to imagine any circumstances in which a seller in a real property sale transaction would want to have a binding letter of intent. A fundamental reality of real estate sales is that the buyer may gain a distinct advantage after the parties enter into a binding letter of intent. The buyer's performance is usually conditional under such an agreement, providing opportunities to terminate the transaction. The seller's position is different: When the seller becomes contractually bound, the property is removed from the market and the seller is subject to a greater risk of an action for specific performance and the recording of a lis pendens if a dispute develops. Thus, it is usually to the buyer's advantage for the letter of intent to be binding—especially in a rising market.

PRACTICE TIP: If circumstances warrant (or the client otherwise insists) that a letter of intent is to be binding, it is essential to include appropriate standards to resolve any issues that may arise and are not addressed in the letter of intent. For example, the following clause should be included: "The final agreement shall contain such other terms and conditions as are customary in contracts for the purchase and sale of similar properties." See form 3.35-2. An arbitration provision to resolve such issues may also be warranted.

© The Regents of the University of California

§3.14 III. RISKS OF USING A LETTER OF INTENT: WHEN IS IT BINDING?

The parties to a letter of intent usually do not intend the letter to constitute a binding contract, but merely to act as a tool for further negotiation. A risk exists, however, that as a result of ambiguous or imprecise drafting, or the subsequent conduct of the parties, the parties signing the letter may be bound to perform a contract found to reside in the letter. Indeed, creating an unintended binding obligation is the primary risk of using a letter of intent.

A binding contract may be found under the theory of waiver or estoppel, however, if the parties' subsequent conduct indicates partial performance or material change in position in reasonable reliance on the letter of intent—even with an explicit statement of no intent to be bound. On estoppel, see §3.26. See also *Monarco v Lo Greco* (1950) 35 C2d 621, 623, 220 P2d 737; *Carlson v Richardson* (1968) 267 CA2d 204, 208, 72 CR 769. On waiver, see *Noel v Dumont Builders* (1960) 178 CA2d 691, 3 CR 220.

The seller's attorney should seriously weigh the risks to the seller of the threat of a specific performance action or a lis pendens.

© The Regents of the University of California

§3.15 A. Unintended Enforceability of Letter of Intent

A court may apply one of three levels of enforceability to a letter of intent otherwise intended to be nonbinding. Depending on how it interprets the parties' intent, the court may treat a letter of intent as creating

- a binding contract between the parties (see §§3.16-3.25);
- a "preliminary commitment," which may be construed to impose on the parties the somewhat uncertain obligation to negotiate further in good faith (see §§3.27-3.30); or
- a basis for a claim of promissory estoppel (see §3.26).

These three levels could be applied to the letter of intent as a whole or to certain clauses only.

PRACTICE TIP: To help avoid the unintended consequences resulting from a court finding enforceable a letter of intent intended to be nonbinding, the attorney should consider providing a liquidated damages provision in the letter of intent (see §3.12 and form 3.35-5).

© The Regents of the University of California

§3.16 1. Objective Manifestation of Mutual Assent

The basic rules of contract formation govern the interpretation of a letter of intent. Every contract requires mutual assent of the parties. CC §§1550, 1565. A letter of intent may be held to constitute a binding contract when the evidence, including the terms of the document and conduct of the parties, shows an objective manifestation of mutual assent. Restatement (Second) of Contracts §§19, 27 (1981).

In describing the competing interests in determining whether a preliminary agreement is binding, the court in *Adjustrite Sys. v GAB Bus. Servs.* (2d Cir 1998) 145 F3d 543, 548, said:

> First, courts must be wary of "trapping parties in surprise contractual obligations that they never intended" to undertake. [Citations.] Second, "courts [must] enforce and preserve agreements that were intended [to be] binding, despite a need for further documentation or further negotiation," for it is "the aim of contract law to gratify, not to defeat, expectations."

In *California Food Serv. Corp. v Great Am. Ins. Co.* (1982) 130 CA3d 892, 897, 182 CR 67, the court enforced a letter of intent because it had all the necessary elements and the parties had performed. In addition to the signed document, the parties' performance "strongly suggest[ed that] both parties considered the terms of the letter of intent as being binding without the need for the execution of additional documents."

In *City of Vernon v Board of Harbor Commissioners* (1998) 63 CA4th 677, 690, 74 CR2d 497, the court construed a "statement of intent" containing the following clause:

> The parties intend this statement to reflect the basic understanding between them, but agree that the transactions contemplated herein shall be subject to the execution of mutually acceptable definitive and final agreements to be negotiated [and] subject to the approval of the [parties]. This statement does not constitute a legally binding commitment.

Under these circumstances, the court found that there could be no expectation of a binding contract. See also *Arcadian Phosphates, Inc. v Arcadian Corp.* (2d Cir 1989) 884 F2d 69 (letter of intent not enforced when it contained express disclaimer of binding effect); *Teachers Ins. & Annuity Ass'n v Tribune Co.* (SD NY 1987) 670 F Supp 491, 498 (letter of intent enforced after exchange of letters constituting commitment agreement stated that borrower and lender had made a "binding agreement").

© The Regents of the University of California

§3.17 2. How to Determine Intent

Under the "objective test" of contract formation, a contract is formed when the parties have manifested by their words or conduct an intent to enter into a mutual agreement. Courts' interpretations of letters of intent are extremely fact specific. Courts have considered some of the following factors relevant to deciding whether the parties intended to be bound by all or part of the letter of intent:

- The parties' conduct (see §3.18);
- Contemplation of formal documents (see §3.19);
- Word choice (see §3.20);
- Specificity (see §3.21);
- Conditional approvals (see §3.22); and
- The complexity and size of the transaction (see §3.23).

For discussion of factors that courts consider in determining the parties' intent, see *Teachers Ins. & Annuity Ass'n v Tribune Co.* (SD NY 1987) 670 F Supp 491.

© The Regents of the University of California

§3.18 a. Parties' Conduct

Courts carefully examine the parties' conduct at the time of and after execution of the letter of intent to ascertain their intent to be bound. Conduct such as celebrations or ceremonies, press releases announcing the transaction, public filings, suspending or forgoing negotiations with others, preparations for performance, or actual performance can indicate the intent to be bound. See, *e.g., Seaman's Direct Buying Serv. v Standard Oil Co.* (1984) 36 C3d 752, 760, 206 CR 354, overruled on other grounds in *Della Penna v Toyota Motor Sales, U.S.A., Inc.* (1995) 11 C4th 376, 393, 45 CR2d 436 (execution of letter was "momentous occasion"; performance begun; letter of intent binding); *California Food Serv. Corp. v Great Am. Ins. Co.* (1982) 130 CA3d 892, 897, 182 CR 67 (performance begun; letter of intent binding); *City of Santa Cruz v MacGregor* (1960) 178 CA2d 45, 54, 2 CR 727 (same).

PRACTICE TIP: To avoid enforcement, the parties should refrain from publicizing the transaction. They may want to add a clause to the letter of intent requiring confidentiality (see form 3.45-1) and avoidance of certain other conduct. If others must be informed of the transaction, the parties should ensure that press releases, public filings, and other notices confirm the nonbinding nature of the letter of intent.

© The Regents of the University of California

§3.19 b. Execution of Formal Documents Expressly Contemplated

A clause in a letter of intent that expressly contemplates the future execution of a formal contract indicates an intent not to be bound (see, *e.g., Beck v American Health Group Int'l* (1989) 211 CA3d 1555, 1562, 260 CR 237) but is not in itself sufficient to ensure that a court will hold the letter to be nonbinding. An ambiguity in this clause allows a court to interpret it as expressing the intent to reduce an obligation to writing rather than the intent not to be bound until the execution of formal documents. See *Arnold Palmer Golf Co. v Fuqua Indus.* (6th Cir 1976) 541 F2d 584, 589. Even the statement that an agreement is "subject to" execution of formal contracts has not always prevented the enforcement of letters of intent. See 541 F2d at 590; *Teachers Ins. & Annuity Ass'n v Tribune Co.* (SD NY 1987) 670 F Supp 491, 499; *Texaco, Inc. v Pennzoil Co.* (Tex App 1987) 729 SW2d 768.

In *City of Santa Cruz v MacGregor* (1960) 178 CA2d 45, 2 CR 727, the parties' signed document said that they would enter into a lease after construction of a building on property "located on Water Street." The building was built, but a lease was never executed. The appellant occupied the property and testified that he thought the original agreement was the only one intended. The court held that the document, conduct of the parties, and testimony would support a finding that the appellant had a valid lease (in spite of vague and missing terms) and so could share in compensation for condemnation of the property by eminent domain.

PRACTICE TIP: To minimize the risk of unintended enforcement, the attorney should include an unequivocal statement that the parties (1) do not intend to be bound until they execute and deliver formal documents or (2) do not intent to be bound by the letter of intent at all. See, *e.g., Roth v Garcia Marquez* (9th Cir 1991) 942 F2d 617; *Skycom Corp. v Telstar Corp.* (7th Cir 1987) 813 F2d 810, 816; *Reprosystem, B.V. v SCM Corp.* (2d Cir 1984) 727 F2d 257, 262; *Chrysler Capital Corp. v Southeast Hotel Prop.* (SD NY 1988) 697 F Supp 794, 801, aff'd without published opinion (2d Cir 1989) 888 F2d 1376. See form 3.35-1.

© The Regents of the University of California

§3.20 c. Language Choice and Verb Tense

Language that contemplates being bound only at an indefinite future time ("we will agree in the future") or use of the subjunctive ("if we were to agree") tends to show that the parties did not intend to be bound by the letter of intent. *Beck v American Health Group Int'l* (1989) 211 CA3d 1555, 1562, 260 CR 237. See also *Arcadian Phosphates, Inc. v Arcadian Corp.* (2d Cir 1989) 884 F2d 69, 72. Conversely, using the present or past tense ("we agree" or "we have agreed" or "accepted and agreed") demonstrates an intent to be bound. See *Harris v Rudin, Richman & Appel* (1999) 74 CA4th 299, 87 CR2d 822. See also *Texaco, Inc. v Pennzoil Co.* (Tex App 1987) 729 SW2d 768; *Itek Corp. v Chicago Aerial Indus.* (Del 1968) 248 A2d 625, 627.

PRACTICE TIP: Clearly, if the parties do not wish to be bound by the letter of intent, this should be stated as explicitly as possible. See §3.19 and suggested language in form 3.35-1. For language and conduct to use or avoid, see §§3.18-3.19, 3.24, 3.30, 3.35.

It is also imperative to avoid using contractual type language such as "offer" and "acceptance" in a letter of intent. The most common error is the inclusion of a final sentence that establishes a deadline for the addressee to "accept" the terms of the letter of intent by a certain date or the terms will be revoked or the letter of intent terminated. Use of this type of contract language arguably shows an intent to enter into a binding agreement.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/3 Letters of Intent/§3.21 d. Specificity of Essential Terms

§3.21 d. Specificity of Essential Terms

Courts may consider the level of specificity as an indication of binding intent. The more specifically the letter of intent addresses the essential terms of the proposed agreement (*i.e.,* the fewer terms left open), the more likely a court will find that the parties intended to be bound. *Computer Sys. v IBM* (1st Cir 1986) 795 F2d 1086. Because the parties' intent is the test, however, lack of specificity in itself will not preclude the court from determining that the parties intended to be bound. *Chrysler Capital Corp. v Southeast Hotel Prop.* (SD NY 1988) 697 F Supp 794, 799, aff'd without published opinion (2d Cir 1989) 888 F2d 1376.

PRACTICE TIP: The language provided in the second paragraph of form 3.35-1 establishes that the letter of intent is not intended to include all of the essential terms of the transaction. It should be included whenever circumstances warrant.

An agreement may be enforced as a final contract even if it is incomplete, *i.e.,* if it contains gaps or open issues. Courts require only that the document either state the essential terms of the agreement (and not necessarily its details or particulars) or provide sufficient information to determine the essential terms. The courts may then supply any open issues by inference from the surrounding circumstances (including prevailing custom and practice) or by operation of law. See, *e.g.,* Com C §2305; *Roth v Garcia Marquez* (9th Cir 1991) 942 F2d 617, 627 (letter of intent that omits essential terms not binding). See also *Okun v Morton* (1988) 203 CA3d 805, 817, 250 CR 220; *Hotel del Coronado Corp. v Foodservice Equip. Distribs. Ass'n* (9th Cir 1986) 783 F2d 1323. Deciding which clauses are "essentials" and which are mere "particulars" is a factual determination based on the surrounding circumstances. 783 F2d at 1325.

© The Regents of the University of California

§3.22 e. Conditional Third Party Approvals

Requirements that the board of directors, legal counsel, or other third parties approve the transaction described in the letter of intent also tend to show an intent not to be bound by a letter of intent. See *A/S Apothekernes Laboratorium v I.M.C. Chem. Group* (7th Cir 1989) 873 F2d 155; *Jewel Cos. v Pay Less Drug Stores NW.* (9th Cir 1984) 741 F2d 1555 (merger agreement subject to shareholder approval was not intended to be legally binding, but board of directors did bind itself to refrain from considering other offers).

Such clauses may, however, be interpreted merely as contractual conditions precedent that the relevant party must attempt to satisfy. For example, failure to seek the approval of the board of directors if the letter of intent is conditioned on such approval may constitute a breach of the implied covenant of good faith and fair dealing (*Jacobs v Freeman* (1980) 104 CA3d 177, 163 CR 680), but even disapproval by the board may be found to have been in bad faith (see *Texaco, Inc. v Pennzoil Co.* (Tex App 1987) 729 SW2d 768, discussed in §3.24).

PRACTICE TIP: Many clients seem to think that simply requiring the approval of the board of directors is sufficient to ensure that a letter of intent will not be binding. It is important to explain that such a condition alone may not achieve that objective. Courts will look to the entire letter of intent and the conduct of the parties to decide the issue. The clause providing that the letter of intent not be binding until approval is granted must be completely unambiguous. See *Arnold Palmer Golf Co. v Fuqua Indus.* (6th Cir 1976) 541 F2d 584, 590; *Teachers Ins. & Annuity Ass'n v Tribune Co.* (SD NY 1987) 670 F Supp 491, 499. The clause should also state that such approval is not the only condition to the transaction and that approval may be granted or withheld in the party's sole and absolute discretion.

© The Regents of the University of California

§3.23 f. Complexity and Size of Transaction

The complexity of the proposed transaction may be a factor in determining whether a court finds a binding contract to have been formed through a letter of intent. In a simple transaction in which the terms and conditions of a letter of intent more or less cover all the expected issues, a court might find that an objective reading of the document does evidence an enforceable contract. By contrast, in a large complex transaction in which the letter of intent can be seen as only hitting the highlights, with numerous issues remaining to be resolved, a finding that a contract was intended may be less likely. *Skycom Corp. v Telstar Corp.* (7th Cir 1987) 813 F2d 810; *Computer Sys. v IBM* (1st Cir 1986) 795 F2d 1086; *Reprosystem, B.V. v SCM Corp.* (2d Cir 1984) 727 F2d 257.

The courts often find that parties do not intend to become engaged in complex transactions without a detailed description of their rights and obligations. *Teachers Ins. & Annuity Ass'n v Tribune Co.* (SD NY 1987) 670 F Supp 491, 503. The author knows of no published opinion by a California court that addresses complexity per se as a determinative factor.

PRACTICE TIP: The sobering result in *Texaco, Inc. v Pennzoil Co.* (Tex App 1987) 729 SW2d 768 demonstrates, however, that one cannot rely on this factor to avoid enforceability. Prudent practitioners make sure that the letter of intent specifically denies an intent to be bound, if this is the desired result. For discussion of *Texaco,* see §3.24.

© The Regents of the University of California

§3.24 3. Unexpected Enforceability in *Texaco v Pennzoil*

Courts may unexpectedly enforce a letter of intent. In *Texaco, Inc. v Pennzoil Co.* (Tex App 1987) 729 SW2d 768, Texaco was found liable for tortious interference with a "memorandum of agreement" on Pennzoil's acquisition of the Getty Oil Company. The court upheld a jury verdict for $10.53 billion against Texaco.

The memorandum of agreement did not include language establishing a binding effect. The press release announcing the proposed acquisition agreement referred to it as an "agreement in principle" for a transaction that was "subject to execution of a definitive merger agreement." 729 SW2d at 789. Unexecuted drafts of the final merger documents stated that the parties' obligations accrued "after the execution and delivery of this agreement." 729 SW2d at 790.

Despite these precautions, the court found sufficient evidence of the parties' intent to be bound by the facts and circumstances surrounding the negotiations to enforce the memorandum of agreement. To support the verdict, the court found the following:

- The press release used indicative language (*e.g.,* "the shareholders will receive") instead of conditional language (*e.g.,* "if we were to agree"), demonstrating an intent to be bound. 729 SW2d at 789.
- The clause, "the transaction is subject to execution of a definitive merger agreement," did not undermine the possibility that the memorandum of agreement was also intended to be a binding agreement. 729 SW2d at 789.
- It was reasonable for the jury to conclude that the phrase "after the execution and delivery of this agreement," which appeared before each of the parties' obligations in the unexecuted merger contracts, merely indicated the timing of various acts and did not condition their occurrence on execution and delivery of the contracts. 729 SW2d at 790.
- The phrase "agreement in principle" was sufficiently ambiguous to support the jury's conclusion that it referred to a binding agreement. 729 SW2d at 791.

Many commentators have disagreed with the holding in *Texaco,* but it provides a clear example of the need for careful analysis and drafting of letters of intent to avoid unintended results. See, *e.g.,* Ranck, *Letters of Intent and Preliminary Agreements*, 6 Corp Couns Q 1 (1990).

PRACTICE TIP: No clear or definitive rule can be drawn from the cases on when a letter of intent will have binding effect. Thus, when drafting or reviewing a letter of intent, the attorney should make sure that it expressly states whether or not the parties intend to be bound by the letter. If they intend to be bound, the letter should clarify to what extent the parties are bound. In addition, the attorney should advise the client after executing the letter to act in conformance with the intent stated in it. Conduct that suggests a different or greater obligation is likely to waive written disclaimers or limitations of binding intent. Including a liquidated damages provision may help neutralize the adverse effects from inconsistent language in a nonbinding letter of intent and conduct by the parties. Although there is no California case on point, if a court finds the letter of intent binding, despite the stated intent not to be bound, then a liquidated damages provision may be enforceable. See form 3.35-5 and Comment to that form.

© The Regents of the University of California

§3.25 4. Statute of Frauds

In addition to the other basic elements of a contract (see §4.12), the Statute of Frauds (CC §§1091, 1624(a)(3); CCP §1971) requires a writing signed by the party to be charged in all sales of real property. Not all terms and conditions of a contract must be contained within the writing to constitute an enforceable contract for the sale of real property. By the terms of the statute, only "some note or memorandum" of the agreement needs to be signed by the party to be charged. Clearly, a letter of intent could be such a "memorandum" because by design it would contain at least the most significant terms. On the Statute of Frauds generally, see §4.13.

For cases in which a court enforced a letter of intent even though it did not conform to the strict requirements of the Statute of Frauds, see *Seaman's Direct Buying Serv. v Standard Oil Co.* (1984) 36 C3d 752, 206 CR 354, overruled on other grounds in *Freeman & Mills v Belcher Oil Co.* (1995) 11 C4th 85, 88, 44 CR2d 420; *Levin v Knight* (9th Cir 1986) 780 F2d 786.

© The Regents of the University of California

§3.26 B. Promissory Estoppel

Promises allegedly made in a letter of intent can be grounds for a promissory estoppel claim. The following are the required elements for promissory estoppel (*Thomson v International Alliance of Theatrical Stage Employees* (1965) 232 CA2d 446, 454, 42 CR 785):

- A clear and unambiguous promise;
- Reliance by the party to whom the promise was made;
- Reasonable and foreseeable reliance; and
- Injury to the party asserting the estoppel as a result of its reliance.

See Restatement (Second) of Contracts §90 (1981).

If the letter of intent clearly shows the parties' intent not to be bound, the writing would tend to negate a clear and unambiguous promise on which the other party could reasonably rely. See, *e.g., Laks v Coast Fed. Sav. & Loan Ass'n* (1976) 60 CA3d 885, 890, 131 CR 836; *Doll v Grand Union Co.* (11th Cir 1991) 925 F2d 1363, 1371; *Reprosystem, B.V. v SCM Corp.* (2d Cir 1984) 727 F2d 257, 264. In *Lange v TIG Ins. Co.* (1998) 68 CA4th 1179, 1186, 81 CR2d 39, when the trial court found that extrinsic evidence was necessary to determine the binding nature of a letter of intent, the court of appeal reversed, holding that "if extrinsic evidence is needed to interpret a promise, then obviously the promise is not clear and unambiguous."

Some courts, however, have accepted the possibility that, even if a letter of intent is not generally binding, some of its provisions could support a promissory estoppel theory. See *Arcadian Phosphates, Inc. v Arcadian Corp.* (2d Cir 1989) 884 F2d 69, 73; *Skycom Corp. v Telstar Corp.* (7th Cir 1987) 813 F2d 810, 817. Further, the nonbinding nature of the letter of intent does not necessarily defeat a theory of promissory estoppel based on oral promises made in connection with or separate from the letter of intent. See *Quan Shew Yung v Woods* (1963) 218 CA2d 506, 32 CR 453, in which the seller's oral approval of a sale, coupled with evidence of a letter from the seller to his agent, and the buyer's reliance (expenditures for improvements) were held to estop the seller from asserting the Statute of Frauds. See also Evid C §623.

Other courts have held that, to support estoppel to assert the Statute of Frauds, the injury suffered by the innocently relying party must be substantial and "unconscionable." See *Allied Grape Growers v Bronco Wine Co.* (1988) 203 CA3d 432, 249 CR 872 (applying Com C §2201, the Statute of Frauds applicable to contract for sale of goods). But see *Isaac v A&B Loan Co.* (1988) 201 CA3d 307, 247 CR 104, in which the buyer's payment of a deposit under an alleged oral agreement to sell real property was not deemed a material change of position or an injury sufficiently unconscionable to support estoppel.

Claims based on promissory estoppel and the duty to negotiate in good faith (see §§3.26-3.30) may arise from similar fact patterns. See *Arcadian Phosphates, Inc.* 884 F2d at 74 (buyer relied on seller's clear, unambiguous promise to negotiate in good faith). Such claims differ, however, with respect to the remedies available. Although breach of the duty to bargain in good faith may allow recovery equal to the full expected return on the contract, promissory estoppel may allow the plaintiff to recoup only actual expenses incurred in reliance on the promise. 884 F2d at 73. See also *Budget Marketing, Inc. v Centronics Corp.* (8th Cir 1991) 927 F2d 421, 428. For an excellent overview on the issue of reliance as a defense, as well as an analysis of what factors justify reliance in the "preliminary agreement" phase, see California Real Property Remedies and Damages §1.53 (2d ed Cal CEB 2002) and Craswell, *Offer, Acceptance, and Efficient Reliance*, 48 Stan L Rev 481, 536 (1996).

PRACTICE TIP: Because parts of a letter of intent could be held to support an estoppel theory and because allegations of collateral promises are always possible, the attorney should include a "no reliance" statement in a letter of intent that is intended to be nonbinding. For suggested language, see form 3.35-1. Also, as a transaction proceeds after execution of a nonbinding letter of intent, the attorney should remain alert for actions or communications that may form the basis of an estoppel claim and take appropriate preventive action when necessary.

© The Regents of the University of California

IV. DUTY TO NEGOTIATE IN GOOD FAITH

§3.27 A. Basis for Existence of Duty

Even if a letter of intent does not establish a binding obligation to carry out the contemplated real estate sale transaction, express or implied terms may obligate a party to negotiate in good faith. See *Copeland v Baskin Robbins U.S.A.* (2002) 96 CA4th 1251, 117 CR2d 875. Before *Copeland* it was unclear whether an agreement to negotiate was enforceable, because some courts characterized such provisions as unenforceable agreements to agree. See *Beck v American Health Group Int'l* (1989) 211 CA3d 1555, 1562, 260 CR 237. See also the discussion in *Vestar Dev. II v General Dynamics Corp.* (9th Cir 2001) 249 F3d 958, 961. *Copeland* holds, however, that "a contract to negotiate an agreement is distinguishable from a so-called 'agreement to agree' and can be formed and breached just like any other contract." *Copeland*, 96 CA4th at 1253.

© The Regents of the University of California

§3.28 B. Necessity of a Contract

In *Copeland v Baskin Robbins U.S.A.* (2002) 96 CA4th 1251, 117 CR2d 875, the court stated that (96 CA4th at 1260)

> [w]hen two parties, under no compulsion to do so, engage in negotiations to form or modify a contract neither party has any obligation to continue negotiating nor to negotiate in good faith. Only when the parties are under a contractual compulsion to negotiate does the covenant of good faith and fair dealing attach, as it does in every contract.

In *Racine & Laramie, Ltd. v Department of Parks & Recreation* (1992) 11 CA4th 1026, 14 CR2d 335, the court held that without a specific agreement imposing an obligation to negotiate in good faith, no such obligation exists. According to the court (11 CA4th at 1034):

> The fact that parties commence negotiations looking to a contract, or to the amendment of an existing contract, does not by itself impose any duty on either party not to be unreasonable or not to break off negotiation, for any reason or for no reason. During the course of negotiations things may be done which do then impose a duty of continued bargaining only in good faith.... For instance… in anticipation of an agreement the parties may, by letter of intent or otherwise, agree that they will bargain in good faith for the purpose of reaching an agreement.

Within the context of an otherwise nonbinding letter of intent, the parties may obligate themselves to "negotiate in good faith," to use "reasonable" or "best" efforts to negotiate a definitive agreement, to "negotiate an agreement containing commercially reasonable terms," or to "negotiate terms that are in accordance with similar transactions in the industry." See *Vestar Dev. II v General Dynamics Corp.* (9th Cir 2001) 249 F3d 958, 962; *Thompson v Liquichimica of Am.* (SD NY 1979) 481 F Supp 365; *Itek Corp. v Chicago Aerial Indus.* (Del 1968) 248 A2d 625, 629. By using this type of language, the parties bind themselves to a duty to negotiate in good faith, thus subjecting themselves to liability or judicial enforcement. In *Copeland v Baskin Robbins U.S.A., supra,* the only language quoted by the court implying an agreement to negotiate was in a letter from Baskin Robbins to Copeland stating Baskin Robbins would agree, "subject to a separate co-packaging agreement and negotiated pricing," to provide Copeland with a 3-year capacity agreement. 96 CA4th at 1254.

© The Regents of the University of California

§3.29 C. Recovery Limited to Reliance Damages

Some courts are reluctant to find that an agreement to negotiate is enforceable, in part because of the difficulty in fashioning a remedy for the breach of such an agreement, especially if expectation damages are sought. See *Budget Marketing, Inc. v Centronics Corp.* (8th Cir 1991) 927 F2d 421; *Arcadian Phosphates, Inc. v Arcadian Corp.* (2d Cir 1989) 884 F2d 69. The court in *Copeland v Baskin Robbins U.S.A.* (2002) 96 CA4th 1251, 117 CR2d 875 (see §3.28) resolved this issue by noting that if an entity breaches its obligation to negotiate (96 CA4th at 1263),

> [t]he plaintiff cannot recover for lost expectations (profits) because there is no way of knowing what the ultimate terms of the agreement would have been or even if there would have been an ultimate agreement.

See also *Auerbach v Great W. Bank* (1999) 74 CA4th 1172, 1191, 88 CR2d 718; *Vestar Dev. II v General Dynamics Corp.* (9th Cir 2001) 249 F3d 958, 961; *Venture Assoc. v Zenith Data Sys.* (7th Cir 1996) 96 F3d 275, 278; and Farnsworth, *Precontractual Liability and Preliminary Agreements: Fair Dealing and Failed Negotiations*, 87 Colum L Rev 217, 263 (1987). The *Copeland* court held that (96 CA4th at 1262)

> damages for breach of a contract to negotiate an agreement are measured by the injury the plaintiff suffered in relying on the defendant to negotiate in good faith. This measure encompasses the plaintiff's out-of-pocket costs in conducting the negotiations and may or may not include lost opportunity costs.

See also *Vestar Dev. II v General Dynamics Corp., supra,* in which the court reasoned that because California case law requires that damages not be speculative—or rather, that they be proved to a reasonable certainty under CC §3301—a breach of an agreement to negotiate cannot be subject to a remedy of lost profits, but only reliance damages such as "time spent, expenses incurred, opportunities foregone, or perhaps harm to its reputation." 249 F3d at 962.

© The Regents of the University of California

§3.30 D. Scope of Duty to Negotiate in Good Faith

In most cases, the question of whether an entity negotiated in good faith will be a question of fact for the jury that "ordinary citizens applying their experience and common sense [are very] well equipped to determine." *Copeland v Baskin Robbins U.S.A.* (2002) 96 CA4th 1251, 1261, 117 CR2d 875 (see §3.28). Meeting the obligation to negotiate in good faith does not necessarily mean that the parties will reach agreement. 96 CA4th at 1257; *Teachers Ins. & Annuity Ass'n v Tribune Co.* (SD NY 1987) 670 F Supp 491, 498. A duty to negotiate in good faith does not prevent a party from bargaining to its own economic advantage, nor does it require parties to conclude the transaction. *Auerbach v Great W. Bank* (1999) 74 CA4th 1172, 1191, 88 CR2d 718, quoting with approval from *Phoenix Mut. Life Ins. Co. v Shady Grove Plaza Ltd. Partnership* (D Md 1990) 734 F Supp 1181, 1190, aff'd without published opinion (4th Cir 1991) 937 F2d 603; *Philmar Mid-Atlantic, Inc. v York St. Assocs II.* (Pa Super 1989) 566 A2d 1253. See also Topinka & Quarterman, *Negotiating and Drafting Engagement Letters Between Investment Bankers and Privately Held Companies*, 6 CEB Cal Bus L Prac 126 (Summer 1990); Restatement (Second) of Contracts §§84, 245-246 (1981) (letter of intent imposes good faith requirement to do everything necessary to complete transaction).

It may be, however, that the determination of whether a person negotiated in good faith will be based on the degree to which that person negotiated in bad faith. In his article cited by the court in *Copeland v Baskin Robbins U.S.A.*, *supra,* Professor Farnsworth identified seven areas that can be considered unfair dealing, including: refusal to negotiate, improper tactics, unreasonable proposals, nondisclosure, negotiation with others, reneging, and breaking off negotiations. See Farnsworth, *Precontractual Liability and Preliminary Agreements: Fair Dealing and Failed Negotiations*, 87 Colum L Rev 217, 273 (1987).

PRACTICE TIP: To avoid a claim based on the duty to negotiate in good faith, the letter of intent should specifically deny the existence of such a duty and state that, unless a definitive agreement is signed, either party may terminate negotiations at any time for any reason or no reason. See form 3.35-1. If negotiations are terminated, the parties can protect against later litigation by acknowledging in writing that, although they did negotiate in good faith, they were unable to reach a final agreement. Alternatively, just as a party may wish to limit any potential damages resulting from a court's determination that a nonbinding letter of intent is binding, a party may also try to limit its damages for any breach of a failure to negotiate in good faith by including a liquidated damages provision in the letter. See §3.12 and form 3.35-5.

PRACTICE TIP: If the parties desire to be bound by the obligation to negotiate in good faith, they should recite that in the letter of intent. See form 3.35-3. They should also include a deadline or time period for the negotiations; otherwise one party may be able to leverage the other party into prolonged negotiations for fear of breaching the obligation to negotiate if the other party ceases to negotiate. See form 3.46-1.

© The Regents of the University of California

V. NEGOTIATING AND DRAFTING A LETTER OF INTENT

§3.31 A. Negotiating and Drafting Considerations

Although the basic business points of a real estate sale transaction are usually left to the principals to negotiate, if a letter of intent is to be used, the form should be drafted by an attorney. As noted in §3.4, important contractual risks must be understood and drafted for in a letter of intent. Business principals are rarely attuned to these issues and may say too little or too much in a letter of intent.

As with any transactional documentation, the party who controls the preparation of the first draft can often achieve a negotiating advantage because the first draft commonly sets the format and content of subsequent discussions and revisions. Thus, the attorney usually advises the client to authorize the attorney to prepare the first draft.

© The Regents of the University of California

§3.32 B. Letter of Intent

The following form illustrates a letter of intent in a transaction for the purchase of an office building. For purposes of this form, assume that the buyer will obtain a new first loan and the seller will take part of the purchase price in the form of a note secured by a second deed of trust on the property.

This form is predicated on the belief that it is best to use a short, simple document. If the circumstances require a long, detailed document, it may be better to forgo a letter of intent and move directly to negotiating and drafting the full contract documentation.

© The Regents of the University of California

§3.33 1. Form: Letter Heading

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§3.33-3.46.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

3.33-1 Letter heading

_ _[*Date*]_ _
_ _[*Name*]_ _
_ _[*Address*]_ _

Re: _ _[*Binding/Nonbinding*]_ _ **Letter of Intent for Purchase and Sale of** _ _[*identify property, e.g., 999 First St. Building*]_ _

Dear _ _[*name of buyer/seller*]_ _**:**

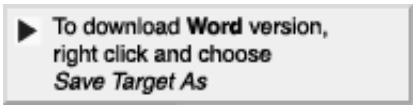
Comment: Identify whether the parties intend the letter of intent to be binding or nonbinding at the very outset of the letter. See §§3.17-3.23.

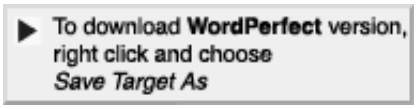
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/3 Letters of Intent/§3.34 2. Form: Introductory Clause

§3.34 2. Form: Introductory Clause

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§3.33-3.46.





3.34-1 Introductory clause

This letter is to serve as a letter of intent between _ _[*name*]_ _ as Seller and _ _[*name*]_ _ as Buyer, stating the preliminary intentions of the parties with respect to negotiating a definite contract for the purchase and sale of real property commonly known as _ _[*address*]_ _ (Property).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/3 Letters of Intent/§3.35 3. Form: Parties' Intentions on Binding or Nonbinding Nature of Letter

§3.35 3. Form: Parties' Intentions on Binding or Nonbinding Nature of Letter

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§3.33-3.46.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

3.35-1 Alternative: Nonbinding letter of intent

This letter of intent is not intended to constitute a binding agreement, but rather to serve as the basis for negotiating and drafting a definitive purchase and sale agreement between the parties containing the terms stated in this letter of intent as well as other terms and conditions to be determined. Neither party will rely on this letter of intent as binding on the other; any such reliance would be imprudent and unreasonable. Neither party will be bound unless and until a definitive agreement has been executed and delivered by both parties and approved by their respective attorneys.

It is understood and agreed that this letter of intent does not contain all the essential terms that the parties expect will be part of an agreement. Further negotiations between the parties are contemplated before a binding agreement will be prepared, but neither party is bound to continue such negotiations, which may be terminated at any time. Further efforts by either party to perform due diligence, arrange or obtain financing, or carry out other acts in contemplation of the possible purchase and sale of the Property may not be deemed evidence of intent by either party to be bound by this letter of intent.

The performance by either party before execution of a formal contract of any of the obligations that may be included in a contract between the parties when negotiations are completed will not be considered evidence of intent by either party to be bound by this letter of intent.

3.35-2 Alternative: Binding letter of intent

The parties contemplate preparation of a more detailed purchase and sale agreement containing additional terms and conditions that are customary for a transaction of the nature contemplated in this letter of intent, but it is understood and agreed that this letter of intent nevertheless binds the parties to the purchase and sale of the Property on the terms and conditions stated in this letter even if a more definitive agreement is not executed.

3.35-3 Alternative: Letter of intent binding only for duty to negotiate in good faith

The parties contemplate preparation of a more detailed purchase and sale agreement containing additional terms and conditions that are customary for a transaction of the nature contemplated in this letter of intent, and they do not intend this letter of intent to constitute a binding agreement for purchase and sale of the Property.

Further efforts by either party to perform due diligence, arrange or obtain financing, or carry out other acts in contemplation of the possible purchase and sale of the Property may not be deemed evidence of intent by either party to be bound by this letter of intent.

The performance by either party before execution of a formal contract of any of the obligations that may be included in a contract between the parties when negotiations are completed will not be considered evidence of intent by either party to be bound by this letter of intent. Despite the foregoing, it is understood and agreed that this nonbinding letter of intent binds the parties to negotiate in good faith for a period of at least _ _[*e.g., 30*]_ _ days for the completion of such a definitive agreement for purchase and sale of the Property.

3.35-4 Alternative: Letter of intent binding for specific obligations

**Except as expressly stated in paragraphs _ _[*insert paragraph numbers of binding clauses*]_ _, titled _ _[*specify*

headings of binding clauses]_ _**, the parties acknowledge and agree that this letter is not intended to be or to evidence any legally binding agreement or obligation on the part of either party. No further agreement will be entered into unless and until each party has reviewed, approved (in its sole discretion), and executed, after review by counsel, a definitive written agreement. Neither party has any obligation to negotiate or conclude the business arrangement described in this letter. Each party acknowledges that it will not take action or refrain from taking action in reliance on the portions of this letter intended to be legally nonbinding and that any such reliance will be at its own risk.**

The parties agree that the provisions in paragraphs _ _[*insert paragraph numbers of binding clauses*]_ _**, titled _ _**[*specify headings of binding clauses*]_ _**, represent the parties' legally binding agreements, enforceable in accordance with their terms. The enforceability of those provisions is not conditioned on further negotiations or the successful outcome of any further negotiations.**

If the parties execute a definitive agreement, that agreement will supersede this letter. Failure to achieve a more complete agreement will not, however, limit the enforceability of the clauses in this letter specified to be binding.

3.35-5 Alternative: Liquidated damages for nonbinding letter of intent

Liquidated Damages for Nonbinding Letter of Intent _ _[*and Breach of Agreement to Negotiate*]_ _

NOTWITHSTANDING THE PARTIES' INTENT THAT THIS LETTER OF INTENT SHALL NOT CONSTITUTE A BINDING AGREEMENT, IF AS A RESULT OF ANY LEGAL ACTION IT IS DETERMINED THAT A PARTY HAS BREACHED ANY OBLIGATION IMPOSED BY THIS LETTER OF INTENT _ _[*(INCLUDING/EXCLUDING ANY OBLIGATION TO NEGOTIATE IN GOOD FAITH, CONFIDENTIALITY, INDEMNIFICATION, INSURANCE, ETC.)*]_ _**, THEN THE PARTIES ACKNOWLEDGE THAT IT WOULD BE EXTREMELY DIFFICULT TO ASCERTAIN THE EXTENT OF ANY DAMAGES RESULTING FROM SUCH BREACH. ACCORDINGLY THE PARTIES AGREE THAT A PAYMENT IN THE AMOUNT OF _ _**[*dollar amount*]_ _ **BY THE BREACHING PARTY TO THE NONBREACHING PARTY SHALL BE THE SOLE DAMAGES AND REMEDY IN THE EVENT OF ANY SUCH BREACH. THIS PROVISION SHALL SURVIVE ANY TERMINATION OF THIS LETTER.**

Initials _____ _____

Comment: It is difficult to imagine any circumstances in which it would be advisable for a seller to use alternative form 3.35-2 or 3.35-3, which bind the seller to sell or to negotiate exclusively the definitive agreement. This agreement would only tie up the property, effectively removing it from the market before the details of an agreement are completed. It is unlikely that the seller's risks of an action for specific performance by the buyer and the threat of a lis pendens recorded against the property would be sufficiently balanced by any benefit of "binding" the buyer by such provisions. Thus, form 3.35-2 is used only rarely in real estate transactions, and clients should be informed of the consequences of entering a binding letter of intent.

As discussed in §§3.27-3.30, the scope, meaning, and potential remedies available for breach of an obligation to negotiate in good faith are not well settled in California. Use of alternative form 3.35-3 attempts to limit the exposure for breaching this obligation by setting a time limit during which the parties are bound to negotiate in good faith.

Form 3.35-4 might be useful if the parties have agreed on a specific obligation, whether or not a definitive agreement for purchase and sale is concluded. See §3.11. For example, if the seller agrees to provide sensitive financial information or environmental reports to the buyer for review before creation of the definitive agreement, the seller may require covenants of confidentiality and return of all documents.

Given the risk that letters of intent drafted with the intent of being nonbinding might be deemed binding by a court (see §§3.14-3.25), adding the liquidated damages alternative form 3.35-5 to nonbinding letters of intent (with the appropriate adjustment to include or exclude any agreement to negotiate in good faith) may serve as a backup provision. If a court finds the letter to be binding, this provision should also be enforceable, thus allowing the parties to limit their exposure to liability to some reasonably agreed sum. Arguably, because the parties intend the letter to be nonbinding, they also do not expect any damages to result from any failure to comply with its terms; thus, a nominal sum should be reasonable. The liquidated damages provision should be sufficient to provide adequate consideration for the parties to be bound by the obligation created by the liquidated damages provision. Note, however, that no California case has addressed a liquidated damages provision in a letter of intent. Thus, practitioners are advised to satisfy the

provisions of CC §§1671-1681 (dealing with the validity of liquidated damages) for a real property purchase contract, such as using 10-point type and initialing.

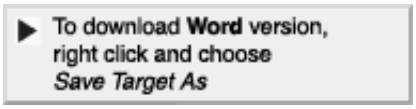
For further examples of binding and nonbinding clauses in letters of intent, see Drafting Business Contracts: Principles, Techniques & Forms, chap 20 (Cal CEB 1994).

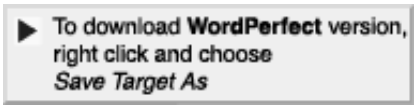
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/3 Letters of Intent/§3.36 4. Form: Description of Property

§3.36 4. Form: Description of Property

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§3.33-3.46.





3.36-1 Description of property

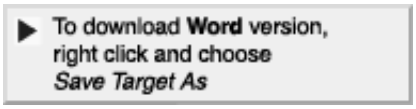
The Property is the land and all improvements located at _ _[*address*]_ _, together with assignment of all leases and contracts pertaining to the Property.

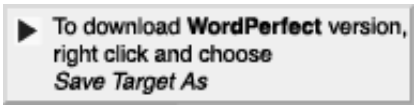
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/3 Letters of Intent/§3.37 5. Form: Purchase Price and Payment of Purchase Price

§3.37 5. Form: Purchase Price and Payment of Purchase Price

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§3.33-3.46.





3.37-1 Purchase price and payment of purchase price

The Purchase Price will be _ _[*dollar amount*]_ _, to be paid _ _[*dollar amount*]_ _ in cash at closing and _ _[*dollar amount*]_ _ under a promissory note secured by a second deed of trust on the Property. The note shall bear interest at the rate of _ _[*number*]_ _ percent annually and will be payable as follows: _ _[*Describe how payments will be made, e.g., $1000 due monthly or annually*]_ _.

© The Regents of the University of California

§3.38 6. Form: Deposits

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§3.33-3.46.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

3.38-1 Deposits into escrow

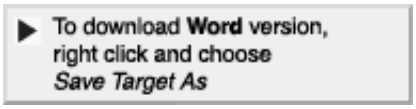
Buyer shall deposit the sum of _ _[*dollar amount*]_ _ in escrow immediately on execution of the definitive purchase agreement. The deposit will be increased to a total of _ _[*dollar amount*]_ _ within _ _[*e.g., 2*]_ _ business days after satisfaction or waiver of Buyer's Contingencies and the Financing Contingency described below. The deposit will be refundable if Buyer elects not to proceed with the purchase as a result of any of Buyer's Contingencies or failure to obtain a loan commitment, but the full deposit will become nonrefundable on satisfaction or waiver of Buyer's Contingencies, except in the case of breach by Seller.

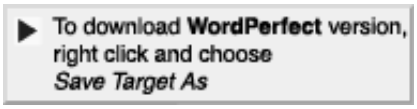
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/3 Letters of Intent/§3.39 7. Form: Purchase and Sale Agreement

§3.39 7. Form: Purchase and Sale Agreement

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§3.33-3.46.





3.39-1 Purchase and sale agreement

Promptly on execution of this letter of intent by Buyer and Seller, _ _[*Seller/Buyer*]_ _'s attorney will prepare and deliver to _ _[*Buyer/Seller*]_ _ a proposed agreement that will include, among other things, the business terms specified in this letter of intent and the provisions in paragraphs _ _[*e.g., 8, 9, 10, 11*]_ _ of this letter of intent. The proposed agreement will not be considered binding unless it is approved and executed by both parties.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/3 Letters of Intent/§3.40 8. Form: Buyer's Contingencies

§3.40 8. Form: Buyer's Contingencies

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§3.33-3.46.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

3.40-1 Conditions precedent to buyer's obligations

The definitive agreement will provide that Buyer's obligations are subject to the following conditions precedent _ _[*and others that may be included on further negotiations*]_ _, the precise statement of which will be subject to the parties' mutual satisfaction (Buyer's Contingencies):

a. Buyer's ability to obtain a first deed of trust loan on the Property in an amount of no less than _ _[*dollar amount*]_ _ on terms and conditions satisfactory to Buyer. Buyer will have _ _[*e.g., 60 days*]_ _ from execution of the definitive agreement in which to obtain a commitment for such loan (Financing Contingency).

b. Buyer's review of and satisfaction with each of the following matters, to be determined within the times stated next to each:

(1) Title to the property: _ _[*e.g., 15 days*]_ _.

(2) Physical inspection, including environmental, engineering, architectural, and other consultants of Buyer's choice: _ _[*e.g., 60 days*]_ _.

(3) All leases and rental agreements: _ _[*e.g., 30 days*]_ _.

(4) Service and maintenance contracts: _ _[*e.g., 30 days*]_ _.

(5) Financial statements, including income and expense statements and rent rolls, certified by Seller as correct: _ _[*e.g., 30 days*]_ _.

(6) All building permits and all inspection reports in the possession of Seller: _ _[*e.g., 30 days*]_ _.

(7) Others: _ _[*Insert any other contingencies and relevant time periods*]_ _.

Comment: As an additional contingency for use if either party (or both) is a partnership, corporation, or other entity, the drafter may wish to add a requirement of evidence that the transaction has been approved by, *e.g.,* the party's partners, board of directors, shareholders. If the letter of intent is binding, such a contingency will include an implied obligation to seek such approval in good faith. See §3.27. See also *Jacobs v Freeman* (1980) 104 CA3d 177, 163 CR 680.

NOTE: The bracketed optional clause in the first paragraph is intended to avoid claims by a party that the list of conditions precedent are exclusive. If the attorney wants to try to limit the conditions precedent to those listed in the letter of intent, this language should be deleted.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/3 Letters of Intent/§3.41 9. Form: Early Access for Inspections

§3.41 9. Form: Early Access for Inspections

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§3.33-3.46.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

3.41-1 Conditions to buyer's right to inspect

Subject to the following terms and conditions, which are intended to be binding on the parties to this letter of intent, Seller agrees to allow Buyer, its employees, agents, or contractors, at Buyer's sole cost and expense, access to the property for the limited purpose of inspections until the earlier of (i) _ _[*e.g. 30 days after the date of the last signatory's execution of this letter*]_ _ or (ii) the termination of negotiations under this letter of intent or (iii) the date on which the parties enter into a definitive agreement regarding the property. The following terms and conditions apply to this period of inspection:

a. The inspections shall only occur during business hours at reasonable times on _ _[*reasonable/number of days*]_ _ advance _ _[*written*]_ _ notice to Seller. All activities undertaken by or on behalf of Buyer in connection with the inspections shall fully comply with applicable laws and regulations, and Buyer shall promptly restore, at its sole cost and expense, any damage arising in connection with the inspections.

b. Before conducting the inspections, Buyer shall submit for Seller's approval a certificate of insurance naming Seller as an additional insured under a commercial general liability policy with _ _[*dollar amount*]_ _ combined single limit for bodily injury and property damage coverage.

c. Buyer may not conduct any intrusive or destructive inspections or borings without Seller's prior written consent, which consent shall be at Seller's sole and absolute discretion.

d. Buyer shall have no right to make inquiries of tenants of Seller or its property manager without Seller's prior consent, which may be conditioned on an agent or representative of Seller accompanying Buyer and its agents or representatives during such inquiries.

e. If the parties do not enter into a definitive agreement regarding the property, Buyer shall furnish Seller with copies of any reports relating to the inspections performed by Buyer or its agents, employees, or contractors, and all such reports shall become Seller's property.

f. Buyer agrees to keep confidential and not to disseminate to any third party, and to cause its agents or representatives to keep confidential and not disseminate to any third party, any information Buyer (and/or its agents or representatives) obtains as a result of the inspections, except to the extent disclosure is required by law. This Paragraph _ _[*e.g., f*]_ _ shall survive the termination of this letter of intent.

g. Buyer hereby releases, indemnifies and agrees to defend and hold Seller free and harmless from and against any and all obligations, lawsuits, injuries, losses, damages, claims, liens, costs, expenses, demands, liabilities, judgments, penalties, investigation costs, including attorney fees and costs, incurred in connection with, arising directly or indirectly out of, or in any way connected with the inspections. Without limiting the generality of this indemnity, Buyer shall (i) keep the property free and clear of any mechanics' or other lien that may be recorded or threatened against the property by any party providing labor, materials, or services in connection with the inspections and (ii) not file or cause to be filed any application or make any request (other than inquiries of the public records) with any governmental or quasi-governmental agency that would or could lead to a hearing before any governmental or quasi-governmental agency or that would or could lead to a note, notice, or violation of law or municipal ordinance, order, or requirement imposed on the property by such an agency, or any change in zoning, parcelization, licenses, permits, or other entitlements or any investigation or restriction on the use of the property, or any part thereof. This Paragraph _ _[*e.g., g*]_ _ shall survive the termination of this letter of intent.

Comment: The provisions of this early access form are seller-oriented and may be subject to some negotiation by the buyer.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/3 Letters of Intent/§3.42 10. Form: Seller's Representations and Warranties

§3.42 10. Form: Seller's Representations and Warranties

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§3.33-3.46.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

3.42-1 Seller's representations and warranties

The definitive agreement will contain the following representations and warranties by Seller _ _[*and others that may be included on further negotiations*]**_ _, the precise statement of which will be subject to the parties' mutual satisfaction:**

a. All documents provided by Seller, including but not limited to rent rolls and financial statements, are true and correct;

b. Seller possesses all licenses, permits, and government approvals necessary for operation of the Property as an office building;

c. The Property is not in violation of any zoning, land-use, environmental, public health, or safety laws;

d. No litigation affecting the Property is pending or currently threatened;

e. Seller has good and marketable title to the Property, and Seller has the unrestricted power and authority to convey the Property to Buyer;

f. The HVAC, plumbing, electrical, mechanical, and other systems of the building will be in good order and operating condition as of the close of escrow;

g. Seller is not aware of any pending or threatened condemnation proceeding affecting the Property;

h. Seller has not discharged or permitted the storage on the Property of any hazardous materials, and Seller is not aware of any discharge or storage or hazardous materials on the Property by any other persons.

Comment: Other representations and warranties might be relevant in a particular transaction. The attorney should also consider which representations and warranties may be unconditional and which may be limited in some way, *e.g.,* "to the best of seller's knowledge" or "to the best of seller's actual knowledge." If such a limitation is used, a definition of its meaning should be added. See §4.107. On seller's representations and warranties generally, see §§4.107-4.120.

NOTE: The bracketed clause in the first paragraph is intended to avoid claims by a party that the list of representations and warranties are exclusive. If the attorney wants to try to limit the representations and warranties to those listed in the letter of intent, this language should be deleted.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/3 Letters of Intent/§3.43 11. Form: Escrow

§3.43 11. Form: Escrow

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§3.33-3.46.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

3.43-1 Establishing escrow and executing escrow instructions

If a definitive agreement is executed by the parties, escrow for this transaction will be established promptly thereafter at _ _[*name*]_ _ Title Insurance Company. Both parties will execute escrow instructions and other instruments necessary to close escrow consistent with the definitive agreement. Escrow will close no later than _ _[*number*]_ _ days after execution of the definitive agreement.

Comment: Closing costs may also be allocated in this clause. On allocation of closing costs generally, see §§15.42-15.46, 15.68-15.70. On escrows generally, see chap 15.

© The Regents of the University of California

§3.44 12. Form: Commissions

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§3.33-3.46.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

3.44-1 Payment of broker's commissions

If the purchase and sale transaction contemplated in this letter of intent is consummated, commissions will be paid as follows: _ _[*Describe, e.g., which party will pay commission, amount of commission, to whom paid, when paid*]_ _**. Nothing in this letter of intent will be deemed to confer any benefit on any third party regarding any claim for commissions.**

Comment: Even if the letter of intent is not binding on the parties, an agreement to pay a commission to the broker may be sufficient to satisfy the Statute of Frauds and give rise to a broker's right to commission, based on a third party beneficiary theory. The final sentence in this form is intended to avoid this problem. For discussion of broker's commissions, see §§2.91-2.123.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/3 Letters of Intent/§3.45 13. Form: Confidentiality

§3.45 13. Form: Confidentiality

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§3.33-3.46.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

3.45-1 Confidentiality

Buyer and Seller agree not to disclose the content of this letter of intent or of any negotiations or information received from the other party regarding _ _[*describe, e.g., the Property, the financial condition of the other party*]**_ _ to any unrelated third parties without first obtaining the prior written consent of the other party.**

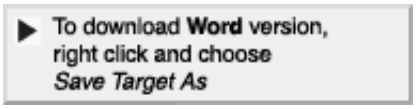
Comment: On the advisability of a confidentiality provision, see §§3.11, 3.18. This clause may be expanded to list specific financial or environmental reports, leases, agreements, or other information that a party wants to remain confidential.

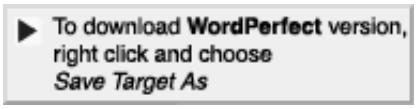
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/3 Letters of Intent/§3.46 14. Form: Execution of Letter of Intent

§3.46 14. Form: Execution of Letter of Intent

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§3.33-3.46.





3.46-1 Alternative: Nonbinding letter of intent

If the foregoing terms correctly state your understanding of the terms on which we will proceed with negotiations for preparation of a purchase and sale agreement, please sign and return the enclosed copy of this letter. As noted above, this letter of intent is not intended to be contractually binding on either party. It will act merely as the basis on which to proceed with further negotiations. If the parties hereto have not entered into a definite purchase and sale agreement with respect to the property within _ _[*e.g., 15 days*]_ _ after the date of this letter, then upon the expiration of such _ _[*e.g., 15-day*]_ _ period any obligation contained in this letter to negotiate or do any other act shall terminate and be of no further force or effect, unless otherwise specifically provided to survive such termination.

Date: _ _ _ _ _ _ _ _[*Name of entity*]_ _,
a _ _[*specify entity, e.g., California corporation*]_ _

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

Approved as of _ _[*date*]_ _**:** _ _[*Name of entity*]_ _,
a _ _[*specify entity, e.g., California corporation*]_ _

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

3.46-2 Alternative: Binding letter of intent

If the foregoing summary of terms forms an acceptable basis on which to proceed with this transaction, please sign and return the enclosed copy of this letter. As noted above, although we intend to negotiate and sign a more definitive purchase and sale agreement, this letter of intent will serve as a binding agreement if no further agreement is completed or executed.

Date: _ _ _ _ _ _ _ _[*Name of entity*]_ _**,**
a _ _[*specify entity, e.g., California corporation*]_ _

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

Approved as of _ _[*date*]_ _**:** _ _[*Name of entity*]_ _**,**
a _ _[*specify entity, e.g., California corporation*]_ _

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

Comment: In alternative form 3.46-1, it is recommended that the parties insert a deadline or time period for their negotiations to avoid an open-ended obligation to negotiate. See §3.30.

Alternative form 3.46-2 should be used with caution and only with letters of intent that the parties intend to be binding.

NOTE: If the client wishes to control the first draft of the document, the execution block of the letter of intent could be expanded to state that, on receipt, the sender will direct his or her attorney to begin drafting the proposed purchase and sale agreement.

© The Regents of the University of California

§3.47 C. Additional Considerations

The letter of intent set forth in §§3.33-3.46 states the principal material terms of the assumed deal. Practitioners will want to consider other potential points that might be included, *e.g.,* the deadline for completion of due diligence, the form of title insurance policy and any endorsements that may be required, inclusion of any particular easements or related rights that may be material to the deal, and representations or warranties of the buyer.

© The Regents of the University of California

4

The Purchase and Sale Agreement

Jennifer R. Bae
Timothy N. Brown
Sherry L. Geyer

I. FORM OF AGREEMENT
- A. Introduction §4.1
- B. Forms and Appendixes §4.2
- C. Conditional Purchase Agreements §4.3
- D. Options §4.4
- E. Use of Printed Forms §4.5

II. ESSENTIAL ELEMENTS OF AGREEMENT
- A. Requirements for Enforceability §4.6
- B. Parties With Capacity to Contract §4.7
- C. Mutual Consent §4.8
- D. Description of Property §4.9
- E. Lawful Object §4.10
- F. Consideration §4.11
- G. Writing
  1. General Rules §4.12
  2. Statute of Frauds §4.13

III. PARTIES
- A. Persons Without Capacity to Contract §4.14
  1. Minors §4.15
  2. Persons of Unsound Mind §4.16
  3. Guardianship or Conservatorship for Persons Under Legal Disability §4.17
- B. Prisoners §4.18
- C. Necessary Parties as Sellers §4.19
- D. Methods of Holding Title
  1. Entities §4.20
  2. Community Property; Cotenancies; Separate Property §4.21
- E. Issues to Consider in Taking Title
  1. Cotenancy
     a. Distinguishing Tenants in Common From Joint Tenants §4.22
     b. Partition of Cotenancy §4.23
  2. General Partnerships §4.24
  3. Limited Partnerships §4.25
  4. Limited Liability Partnerships §4.26
  5. Limited Liability Companies §4.27
  6. Corporations §4.28

IV. INTRODUCTORY PROVISIONS OF AGREEMENT
- A. Preamble and Recitals §4.29
- B. Agreement to Buy and Sell §4.30
- C. Description of Property
  1. Legal Description of Real Property §4.31
  2. Improvements and Appurtenances §4.32
  3. Personal Property §4.33
  4. Intangible Property §4.34

V. PURCHASE PRICE AND DEPOSIT
- A. Price
  1. Type of Consideration §4.35

2. Allocation of Purchase Price §4.36
B. Deposit §4.37
C. Purchasing Subject to Existing Encumbrances
1. Credit to Purchase Price §4.38
2. Review of Loan Documents
a. In General §4.39
b. Issues in Securitized Loans §4.40
3. Buyer's Personal Liability
a. Assuming Encumbrances §4.41
b. Taking Subject to Encumbrance §4.42
4. Due-on-Sale Provision §4.43
D. Seller Financing §4.44

VI. DUE DILIGENCE §4.45
A. Methods of Providing for Due Diligence §4.46
B. Due Diligence Conditions
1. Purpose of Due Diligence Conditions §4.47
2. Drafting Considerations §4.48
C. Seller's Disclosure Obligations §4.49
D. Title
1. Marketable Title
a. Definitions of Marketable Title §4.50
b. Examples of Unmarketable Title §4.51
c. Statutory Procedures for Curing Certain Title Defects §4.52
2. Title Insurance §4.53
a. Preliminary Report
(1) Contents of Preliminary Report §4.54
(2) Nature of Preliminary Report §4.55
(3) Fees and Costs §4.56
b. Purchase Agreement's Title Insurance Provisions §4.57
3. Surveys
a. Role of Surveys §4.58
b. Seller's Knowledge and Notice of Boundaries §4.59
4. Typical Title Issues
a. Taxes
(1) Real Property Taxes §4.60
(2) Personal Property Taxes §4.61
(3) Federal Tax Liens §4.62
b. Special Assessments §4.63
c. Easements §4.64
d. Party Walls §4.65
e. Covenants, Conditions, and Restrictions §4.66
f. Encroachments §4.67
g. Adverse Possession §4.68
h. Mechanics' Liens §4.69
i. Matters Discoverable by Inspection §4.70
E. Leases
1. In General §4.71
2. Purchase Free of Leases §4.72
3. Purchase Subject to Leases §4.73
4. Agricultural Leases §4.74
5. Ground Leases §4.75
6. Third Party Contracts §4.76
F. Physical Condition of Property
1. In General §4.77
2. Buyer's Inspection Rights §4.78
3. Structural Pest Control Inspection §4.79
4. Hazardous Substances §4.80
5. Natural Hazard Disclosure Statement §4.81
6. Toxic Mold Disclosure Requirements §4.82
G. Financing §4.83
H. Seller's Books and Records §4.84
I. Use and Development of Property
1. In General §4.85
2. Zoning §4.86

3. Conditional Use Permits and Variances §4.87
4. Coastal Development Permits §4.88
5. Other Permits §4.89
6. Access §4.90
7. Annexation §4.91
8. Subdivision §4.92
9. Williamson Act §4.93
10. California Environmental Quality Act §4.94
a. Requirement for Environmental Review §4.95
b. Exemptions and Negative Declarations §4.96
c. Environmental Impact Reports (EIRs) §4.97
d. Impact on Buyer §4.98
J. Failure to Meet Due Diligence Conditions
1. Issues Regarding Failure of Conditions §4.99
2. Recovery of Buyer's Deposit §4.100

VII. COVENANTS PENDING CLOSING
A. Leases
1. Covenant by Seller to Obtain Estoppel Certificates §4.101
2. Limitations on New Leases §4.102
3. Seller's Obligation to Terminate Leases §4.103
B. Seller's Operations of Property §4.104
C. Seller's Construction Covenants §4.105
D. Insurance §4.106

VIII. REPRESENTATIONS AND WARRANTIES
A. Purpose §4.107
B. Limitations on Warranties §4.108
C. Survival of Warranties §4.109
D. Trend Toward Limited Warranties §4.110
E. Typical Subjects for Seller's Warranties
1. Title §4.111
2. Physical Condition of Property §4.112
3. Zoning §4.113
4. Subdivision Map Act Compliance §4.114
5. Violation of Other Governmental Requirements §4.115
6. Litigation §4.116
7. Books, Records, Leases, and Contracts §4.117
8. Authority §4.118
F. Typical Buyer's Warranties §4.119
G. "As Is" Provisions §4.120

IX. CLOSING CONDITIONS
A. Purpose of Closing Conditions §4.121
B. Typical Buyer's Conditions
1. Title Insurance §4.122
2. Other Conditions §4.123
C. Typical Seller's Conditions §4.124
D. Releases and Waivers by Buyer §4.125
E. Closing Subject to Another Transaction §4.126
1. Simultaneous Exchange §4.127
2. Multiple Sellers §4.128
3. Removal of Title Defect §4.129
4. Purchase of Additional Property §4.130
5. Sale of Another Property by Buyer §4.131

X. ESCROW AND CLOSING
A. Closing Through Escrow §4.132
B. Prorations §4.133
C. Closing Costs §4.134
D. Brokerage Fees §4.135
E. Possession §4.136

XI. RISK OF LOSS §4.137

A. Condemnation Loss §4.138
B. Casualty Loss §4.139

XII. DEFAULT AND REMEDIES
A. In General §4.140
B. Seller's Remedies
1. Damages §4.141
2. Liquidated Damages §4.142
3. Specific Performance §4.143
C. Buyer's Remedies
1. Damages §4.144
a. Civil Code §3306 §4.145
b. Civil Code §3300 §4.146
c. Fraud and Misrepresentation §4.147
2. Methods to Limit Buyer's Damages §4.148
3. Specific Performance §4.149
D. Alternative Dispute Resolution §4.150

XIII. MISCELLANEOUS PROVISIONS
A. Notices §4.151
B. Time Is of the Essence §4.152
C. Attorney Fees §4.153
D. Waiver §4.154
E. Assignment by Buyer §4.155
1. Entity to be Formed §4.156
2. Use of Nominees §4.157
F. Interpretation of Agreement §4.158
1. Integration Provision §4.159
2. Counterparts §4.160
3. Binding on Successors §4.161
G. Amendments Only in Writing §4.162
H. No Third Party Benefit §4.163
I. Severability §4.164
J. Tax-Deferred Exchange §4.165

XIV. PURCHASE AND SALE AGREEMENT §4.166
A. Form: Title and Introductory Paragraph §4.167
B. Form: Recitals §4.168
C. Form: Agreement of Sale §4.169
D. Form: Purchase Price §4.170
E. Form: Buyer's Contingencies §4.171
F. Form: Seller's Preclosing Covenants §4.172
G. Form: Representations and Warranties §4.173
H. Form: Closing Conditions §4.174
I. Form: Closing §4.175
J. Form: Risk of Loss §4.176
K. Form: Remedies for Default §4.177
L. Form: General Provisions §4.178
M. Form: Signature §4.179
N. Form: Consent of Escrow Holder §4.180
O. Form: Table of Exhibits §4.181
P. Form: Allocation of Purchase Price §4.182

© The Regents of the University of California

I. FORM OF AGREEMENT

§4.1 A. Introduction

Purchase and sale agreements for all types of real property are covered in detail in this chapter. The purchase and sale of residential properties have additional requirements, which are discussed in chap 6. When preparing to represent a client for a residential transaction, counsel must review both chapters.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.2 B. Forms and Appendixes

§4.2 B. Forms and Appendixes

A purchase and sale agreement with both buyer- and seller-oriented alternative provisions is presented in §§4.166-4.182. The agreement is illustrative and should be adapted for the particular circumstances. The provisions of the form follow the same order as the discussion of the issues in this chapter.

The appendixes include the following:

- A table describing the transfers that trigger reappraisals (see App A);
- Two checklists for commercial property transactions:
- Buyer's checklist for acquisition of commercial property and due diligence (see App B), and
- Checklist of due diligence materials to be delivered by a seller to a buyer in a sale of a property with commercial leases (see App C);
- Examples of documents typically delivered at closing of a commercial real estate transaction:
- Board of directors resolution authorizing purchase for a corporation (see App D),
- Limited liability company certificate authorizing the purchase (see App E), and
- Statement of partnership authority for a general partnership (see App F);
- Documents conveying title to various assets:
- Grant deed (see App G),
- Bill of sale for personal property (see App H),
- Assignment of leases (see App I), and
- Assignment of intangible property (see App J);
- Documents for use in transactions involving commercial leases:
- Estoppel certificate from tenants (see App K), and
- Letter to tenants after closing directing them to pay rent to the new buyer (see App L);
- Waiver to be executed by the nonowner spouse when his or her wife or husband sells property owned separately (see App M);
- Alternative form of disclosure of natural hazard conditions on the property to be sold—a seller of commercial property may prefer to use this form instead of the form used for residential property sales (see App N); and
- Tenancy in common agreement (see App O).

Examples of other types of documents and provisions used in connection with real property sales are in other chapters of this book; see the Table of Forms.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.3 C. Conditional Purchase Agreements

§4.3 C. Conditional Purchase Agreements

In a bilateral contract, the parties' promises must be mutual in obligation; thus, for the contract to bind either party, both must have assumed some legal obligations. If one party is free to perform or not, without even a good faith requirement, that party's promise is illusory and affords no consideration: it is a free and revocable option. *Shortell v Evans-Ferguson Corp.* (1929) 98 CA 650, 277 P 519.

The good faith implied in a contract, however, may be sufficient to overcome the claim of lack of consideration. In *Mattei v Hopper* (1958) 51 C2d 119, 330 P2d 625, a sale conditioned on obtaining leases "satisfactory" to the buyer was held to be binding because the buyer's satisfaction is not unfettered but must meet the legal standard of reasonableness or good faith, depending on the nature of the performance. Later decisions upheld contracts conditioned on the buyer's satisfaction with results of a test of a well (*Lyon v Giannoni* (1959) 168 CA2d 336, 335 P2d 690) and with a subdivision map as finally approved (*Rodriguez v Barnett* (1959) 52 C2d 154, 338 P2d 907).

In *Peak-Las Positas Partners v Bollag* (2009) 172 CA4th 101, 90 CR3d 775, a purchase agreement provided for escrow to close on approval of a lot line adjustment and no later than 2 years from the opening of escrow unless the buyer and seller mutually agreed to extend the agreement. Governmental requirements delayed the project and the parties further extended the escrow after an additional deposit by seller. At the expiration of this extension, the seller denied a further extension, pleading in part that he feared the project would never be approved. The buyer by this time had paid 98 percent of the purchase price and spent $5 million in project costs and was diligently trying to obtain a lot line adjustment. The court found that the seller had acted unreasonably and in bad faith in denying consent to the escrow extension and had breached the purchase contract.

If the condition can be measured by an objective standard, as in financial or structural considerations, the party's satisfaction must meet the "reasonable person" test. *Mattei v Hopper, supra*; *Kadner v Shields* (1971) 20 CA3d 251, 97 CR 742. If the party's satisfaction depends on matters of taste or judgment, however, the courts require that the party act in good faith. *Kadner v Shields, supra*. A contract does not fail for lack of consideration or mutuality of obligations because a buyer may approve or disapprove a condition in buyer's sole judgment or discretion. The buyer must, however, exercise such judgment and discretion within the constraints of the implied contractual duty of good faith and fair dealing. See *Larwin-Southern California v JGB Inv. Co.* (1979) 101 CA3d 626, 162 CR 52. For a general discussion of the covenant of good faith, see Drafting Business Contracts: Principles, Techniques & Forms §9.23 (Cal CEB 1994).

A condition, such as obtaining financing, may be held to include an implied covenant that the party it was intended to benefit will use due diligence in attempting to fulfill the condition. *Abrams v Motter* (1970) 3 CA3d 828, 83 CR 855; *Fry v George Elkins Co.* (1958) 162 CA2d 256, 327 P2d 905. It is the seller's burden to prove the buyer's lack of due diligence, but if the buyer admits lack of diligence, the burden shifts to the buyer to prove that the condition could not have been fulfilled in any event. *Abrams v Motter, supra.* In certain instances, the seller might want to retain the right to obtain performance of the condition if the buyer is unable to do so. Similarly, if the party who controls the occurrence of the condition is required by the agreement to take specific steps in attempting to achieve the condition, courts are likely to find sufficient consideration for mutuality. See *White & Bollard, Inc. v Goodenow* (Wash 1961) 361 P2d 571; Note, *Contracts: Consideration: Effect of Clauses in Real Estate Contracts Conditioning Buyer's Promise*, 47 Cal L Rev 753 (1959).

PRACTICE TIP: To avoid an argument regarding mutuality, if the agreement is contingent on the occurrence of a condition that is under the control of a party who is not obligated to actually achieve the condition, then the agreement should obligate the party to perform certain acts in meeting the condition, or should impose standards of reasonableness on the exercise of any approval rights. In any event, the agreement should state that the party is merely obligated to attempt to meet the condition and should negate the implication that the party is actually required to meet it. See 1 Friedman on Contracts and Conveyances of Real Property, chap 1 (7th ed 2006).

The general rule is that a party may waive a condition that is solely for that party's benefit and obtain performance of the agreement. *Doryon v Salant* (1977) 75 CA3d 706, 142 CR 378. Such a party may be deprived of the right to waive

the condition in certain circumstances, *e.g.,* automatic termination. Automatic termination takes place if the agreement provides that it is "void" or that it "ceases and terminates" on the failure of performance of a condition. *Nikora v Mayer* (2d Cir 1958) 257 F2d 246.

PRACTICE TIP: Parties who wish to reserve the right to waive conditions included for their benefit should provide that they may terminate or proceed at their discretion on the occurrence or failure of the condition.

Unless the agreement expressly permits it, one party cannot waive a condition that is for the benefit of both the buyer and the seller. An example is a condition requiring FHA approval for development, which would enhance the value of the property as security for the seller's purchase money deed of trust. *Spangler v Castello* (1956) 147 CA2d 49, 304 P2d 752. When the rights of a tenant with an option to purchase are to be eliminated, waiver of that condition by the buyer alone does not suffice, because the seller would be liable to the tenant. *Britschgi v McCall* (1953) 41 C2d 138, 257 P2d 977.

In some instances, the seller's actions may deprive the buyer of the election to waive a condition.

EXAMPLE: If the buyer adds to the purchase agreement a condition that it is subject to the buyer's ability to obtain financing, without indicating the source, the seller may be able to bind the buyer by agreeing to take back a purchase money deed of trust on the same terms. This procedure could be disadvantageous to the buyer because the seller may be more difficult as a creditor than a third party, such as an institution with established practices. To avoid this result, the buyer should make sure that the agreement gives the buyer the sole option on third party financing.

© The Regents of the University of California

§4.4 D. Options

A number of California lawyers advocate options that enable buyers to tie up property while investigating it without being bound to buy it. One option permits the seller to retain the deposit as the price for the option if it is not exercised, thus avoiding problems of liquidated damages. Options are discussed in more detail in chap 8. See *Patel v Liebermensch* (2008) 45 C4th 344, 86 CR3d 366 (discussion of specific performance of real estate option contract). See §4.142 for requirements for liquidated damages provisions.

© The Regents of the University of California

§4.5 E. Use of Printed Forms

Counsel should carefully review printed forms provided by brokers, title companies, escrow agents, and stationery stores before using them. The advantage of using these forms is that a printed form has a certain authority, some clients accept them readily, and the work needed to amend a form (and resulting cost to the client) may be less than that required to prepare an entire agreement. Many such forms, however, contain provisions that may be objectionable, such as a provision that title is to be taken by the buyer "subject to covenants, conditions, and restrictions of record" or "subject to any state of facts an accurate survey would reveal." If printed forms are used, they should be read carefully to ascertain the propriety and adequacy of their provisions for a particular transaction and their compatibility with the addendums so that the agreement as a whole is consistent and clear. Lawyers who are familiar with a printed form should not assume they know what it says; with laser printers a document can be produced that looks familiar but that has actually been modified. See §§1.119-1.120 on use of printed forms. On reconciling inconsistencies between printed provisions and addendums, see §2.62. For form provisions, see §§2.64-2.88.

TAX CONSIDERATIONS: Many printed forms do not properly consider tax issues, particularly California real property taxes and documentary transfer taxes. Mistakes or omissions in these areas can amount to more than the cost savings in using a preprinted or boilerplate form.

© The Regents of the University of California

II. ESSENTIAL ELEMENTS OF AGREEMENT

§4.6 A. Requirements for Enforceability

The essential elements of an enforceable contract are these (CC §1550):

- The parties' capacity to contract;
- The parties' mutual consent;
- A lawful object; and
- Sufficient consideration.

Agreements for the sale of real property must meet the additional requirement that the agreement, or a memorandum of it, must be in writing and signed by the party to be bound. CC §1624(a)(3). The buyer's agreement "to pay an indebtedness secured by a mortgage or deed of trust upon the property" must also be in writing. CC §1624(a)(6). To obtain specific performance, the agreement must be sufficiently certain (CC §3390(5)), which requires designating the parties, the purchase price, the method of payment, and the description of the property (see 5 Witkin, California Procedure, *Pleading* §787 (5th ed 2008)).

© The Regents of the University of California

§4.7 B. Parties With Capacity to Contract

To create an enforceable contract, the parties must be capable of contracting. CC §1550. All persons are capable of contracting except minors, persons of unsound mind, and persons deprived by law of their civil rights. CC §1556. The word "person" includes a corporation as well as a natural person. CC §14. Under Corp C §§16204 and 16302, a partnership may also contract in the firm's name concerning property. On partnerships, see §§4.24-4.26. Limited liability companies also have all the powers of a natural person, including the power to make contracts, purchase and sell real property, and transfer or otherwise dispose of their property. Corp C §17003. On limited liability companies, see §4.27. On corporations, see §4.28.

© The Regents of the University of California

§4.8 C. Mutual Consent

The consent of the parties to a contract must be free, mutual, and communicated by each to the other. CC §1565. Consent that is not free can be rescinded. CC §1566. See California Real Property Remedies and Damages, chap 1 (2d ed Cal CEB 2002) on rescission. Consent is not real or free if it is obtained through duress, menace, fraud, undue influence, or mistake, and if it would not have been given if that cause had not existed. CC §§1567-1568; see Real Property Remedies, chap 3, on remedies for fraud. Mutual assent is also lacking if the contract is so ambiguous that the parties' intentions cannot be ascertained. On uncertainty, see Real Property Remedies §4.19.

Mistake may, in rare instances, prevent a contract from coming into existence. For example, if the parties have a different understanding of the subject matter, and if neither is at fault or both are equally at fault, there is no contract. *Barfield v Price* (1871) 40 C 535. Usually, however, mistake does not prevent the formation of a contract but makes it voidable.

On reformation, see Real Property Remedies, chap 2.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.9 D. Description of Property

§4.9 D. Description of Property

The description of the property in the agreement must be sufficiently certain to satisfy the Statute of Frauds (CC §1624(a)(3); CCP §1971) and to make the agreement specifically enforceable (CC §3390(5)). For certainty in descriptions generally, see §§4.31-4.34, 11.14-11.21. For certainty in partial releases of land from deeds of trust, see §§9.100-9.104. On uncertainty as a defense to an action for breach, see California Real Property Remedies and Damages §4.19 (2d ed Cal CEB 2002).

© The Regents of the University of California

§4.10 E. Lawful Object

The object of a contract must be lawful at the time the contract is made. CC §§1550(3), 1596. A contract's object is the performance that the party receiving the consideration agrees to provide. When a contract has but one object and that object is unlawful, the contract is void (CC §1598); but when a contract has several objects, it is void only to the extent that any particular object is unlawful (CC §1599). Unlawfulness is defined as that which is "(1) contrary to an express provision of law; (2) contrary to the policy of express law, though not expressly prohibited; or (3) otherwise contrary to good morals." CC §1667.

© The Regents of the University of California

§4.11 F. Consideration

To support a claim in damages for breach or an assertion that the buyer is a bona fide purchaser, an agreement must be based on good (*i.e.,* valuable) consideration. See *Horton v Kyburz* (1959) 53 C2d 59, 346 P2d 399. Any benefit conferred or detriment suffered (or agreed to be conferred or suffered) is good consideration if it is more than nominal. See CC §1605. If the agreement is to be specifically enforced, however, the consideration must also be adequate (*i.e.,* it must be just and reasonable). CC §3391(2). On specific performance, see §4.143. In both situations, the value or adequacy of the consideration is fixed as of the time the agreement is executed. *O'Connell v Lampe* (1929) 206 C 282, 274 P 336; *Henderson v Fisher* (1965) 236 CA2d 468, 46 CR 173.

© The Regents of the University of California

G. Writing

§4.12 1. General Rules

A contract for the sale of an interest in real property must be evidenced by a writing "subscribed" by the party to be charged. CC §1624(a)(3); CCP §1971. The subscription need not be a handwritten signature but may be typed, printed, or stamped, and it may be initials or any other form, as long as it is intended as the execution. *Weiner v Mullaney* (1943) 59 CA2d 620, 140 P2d 704.

NOTE: The Uniform Electronic Transactions Act (CC §§1633.1-1633.17) provides that an instrument or a document in electronic form—an electronic record ("a record created, generated, sent, communicated, received, or stored by electronic means") or electronic signature—satisfies the legal requirement of a writing or signature. See also the federal Electronic Signatures in Global and National Commerce Act (15 USC §§7001-7031) (Pub L 106-229, 114 Stat 464) regarding signatures for agreements made electronically.

If the writing is subscribed by an agent, written authority must be subscribed by the principal. CC §1624(a)(3). The agent's authority to sign need not be in writing when the act is purely clerical or ministerial, *e.g.,* when the agent is directed by the principal to sign the document for the principal. *Murphy v Munson* (1949) 95 CA2d 306, 212 P2d 603.

A distinction must be made between the statutory requirement that the agreement be signed by the person to be charged and the effect of the parties' understanding that no agreement exists until both parties sign a formal agreement. *Stromer v Browning* (1966) 65 C2d 421, 55 CR 18; *Apablasa v Merritt & Co.* (1959) 176 CA2d 719, 1 CR 500. When the parties intend the latter to occur, both parties must sign and the agreement must take the form intended by the parties before an enforceable contract exists. See also *Fugate v Cook* (1965) 236 CA2d 700, 46 CR 291 (husband's signature to agreement ineffective if conditioned on wife's signature). But see *Angell v Rowlands* (1978) 85 CA3d 536, 149 CR 574 (husband bound on contract of sale not signed by wife without a showing that contract was not intended to be complete until signed by all parties named in it).

Letters of intent present special problems of enforceability as written agreements. See chap 3.

© The Regents of the University of California

§4.13 2. Statute of Frauds

To satisfy the Statute of Frauds, the writing need not be a formal agreement but may be in the form of a letter, memorandum, or telegram. It must contain the essential elements of a contract, *i.e.,* the names of the buyer and the seller and their identification (on parties to the contract generally, see §§4.7, 4.14-4.28), a description of the property (see §§4.31-4.34, chap 10), the price, and the time and manner of payment (see §§4.35-4.44). *Corona Unified Sch. Dist. v Vejar* (1958) 165 CA2d 561, 332 P2d 294. But see *House of Prayer v Evangelical Assoc. for India* (2003) 113 CA4th 48, 7 CR3d 24 (time for performance is not essential term in every contract, and if no time is given, court may imply reasonable time for performance). It is best to reduce the agreement to a formal document to avoid ambiguities and inadequacies.

Despite the somewhat contrary language of CC §1624, courts have uniformly held that noncompliance with the Statute of Frauds renders a contract unenforceable rather than void. An oral contract subject to the statute is effective until its invalidity is urged as a defense to an attempt to enforce it. 1 Witkin, Summary of California Law, *Contracts* §344 (10th ed 2005). Thus, the statute's use is primarily defensive. For example, it cannot be invoked by a buyer to recover payments made under an oral contract to sell land if the seller is ready and able to perform. *Walbridge v Richards* (1931) 212 C 408, 298 P 971; *Thompson v Schurman* (1944) 65 CA2d 432, 437, 150 P2d 509. Moreover, part performance of an oral contract may be sufficient to overcome even defensive use of the Statute of Frauds. CCP §1972. In some cases, a party may be estopped from asserting the Statute of Frauds as a defense.

EXAMPLE: In *Sutton v Warner* (1993) 12 CA4th 415, 15 CR2d 632, tenants in possession entered into an oral lease with an option to buy. They made a substantial downpayment, increased their monthly rent to the precise amount of the monthly mortgage payment, semiannually reimbursed the owners for property taxes, and made many improvements to the property. When the property appreciated in value, the owners tried to get a higher sales price, but the court enforced the tenants' version of the oral contract, holding that their continued possession of the property and other actions were sufficiently related to the oral option contract to constitute part performance and defeat the bar of the Statute of Frauds.

Some real property contracts do not require a writing, including the following (1 Witkin, Summary, *Contracts* §385):

- An agreement to share the profits of a sale of real property;
- A partnership agreement to deal in real property;
- A license to use real property;
- An agreement settling a disputed boundary;
- A fully executed partition agreement; and
- A sale of growing crops or mining rights.

© The Regents of the University of California

III. PARTIES

§4.14 A. Persons Without Capacity to Contract

As noted in §4.7, an essential element of a contract is that the parties have the legal capacity to contract. The major classifications of persons without capacity to contract are minors, persons of unsound mind, persons with a legal disability, and certain prisoners.

© The Regents of the University of California

§4.15 1. Minors

An individual under age 18 is a minor (Fam C §6500) and cannot make a contract relating to real property or to any interest in real property (Fam C §6701(b)). Such contracts are absolutely void and thus need not be disaffirmed. *Sparks v Sparks* (1950) 101 CA2d 129, 225 P2d 238. Not only are such contracts void from their inception, but it has been held that the minor need not even return the consideration. *Sparks v Sparks, supra.* (Apparently, the only protection even a bona fide purchaser has against any conveyance by a minor is a claim against the title insurance policy or a claim to the property by adverse possession if the buyer, or the buyer's predecessor in interest, has held the property for at least 5 years after the minor reached majority.)

A minor can hold title to real property because the law presumes acceptance of a beneficial grant. *People v Fujita* (1932) 215 C 166, 8 P2d 1011; *Estate of Yano* (1922) 188 C 645, 206 P 995. A transfer of title to real property held by a minor requires the appointment of a guardian. See §4.17. An emancipated minor, however, does have the power to buy, sell, lease, encumber, exchange, or transfer an interest in real property. Fam C §7050(e)(3). An emancipated minor is one who has entered into a valid marriage, whether or not such marriage was terminated by dissolution, who is on active duty with the United States Armed Forces, or who has received a declaration of emancipation under Fam C §7122. Fam C §7002.

© The Regents of the University of California

§4.16 2. Persons of Unsound Mind

Persons of unsound mind are classified in two categories: those entirely without understanding (CC §38) and those of unsound mind but not entirely without understanding (CC §39). The former have no power to make a contract, and any contracts they make are void. *Estate of McConkey* (1939) 33 CA2d 554, 92 P2d 456. Contracts of persons defined in CC §39, made before judicial determination of their incapacity, are subject to rescission. CC §§39, 1689(b)(7). If incompetence is judicially determined, no conveyance or other contract is valid unless it is made after the incompetent is restored to capacity. CC §40; *Carroll v Carroll* (1940) 16 C2d 761, 108 P2d 420.

© The Regents of the University of California

§4.17 3. Guardianship or Conservatorship for Persons Under Legal Disability

Although minors and incompetents lack the capacity to convey property, a guardian or conservator who is properly authorized may do so in their name. Prob C §2420(b); *Estate of Kay* (1947) 30 C2d 215, 181 P2d 1. The California guardian and conservatorship law is in Prob C §§1400-3803. See also California Conservatorship Practice §§17.28-17.83 (Cal CEB 2005) for discussion of conservatorship procedures regarding real property.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.18 B. Prisoners

§4.18 B. Prisoners

Civil rights of persons incarcerated in a state prison may be subject to suspension during their imprisonment but are not forfeited. Pen C §2600. A prisoner has the right to own, sell, or convey real property, but the Department of Corrections may restrict or prohibit sales or conveyances that are made for business purposes. Pen C §2601(a). If one party to an agreement is in a state prison, the other party should verify that the prisoner has a right to enter into the agreement.

© The Regents of the University of California

§4.19 C. Necessary Parties as Sellers

Before preparing a purchase and sale agreement, counsel must know who has to sign it. To ascertain this, the lawyer for the seller must know who has an interest in the property. (It is preferable to do this preliminary title work before the agreement is signed, to be sure that all persons who own an interest in the property are made parties to the agreement.) See §1.66. A party who signs an agreement to sell an interest greater than that actually owned is liable for both specific performance for the interest that he or she has and damages to the buyer if title to the interest sold cannot be delivered. *Armstrong v Sacramento Valley Realty Co.* (1921) 52 CA 110, 115, 198 P 217. Seller's counsel should review title to ensure that title can be delivered free of all encumbrances other than any the buyer will take subject to under the agreement.

To learn who holds title and to make sure that the seller can deliver the agreed title, counsel must consider issues such as these:

- If the seller was married when the property was acquired or if a marriage occurred later, the spouse should also sign the agreement (see Fam C §1102(a)) or execute and record a power of attorney in favor of the other spouse.
- If the selling spouse claims that the property is separate property, the other spouse should execute a quitclaim deed or a waiver like the one in App M.
- If the property has been declared a homestead, all owners of homestead rights should join in the agreement. The spouse of an owner declaring a homestead on the owner's own separate property for their joint benefit has an interest in the property. CCP §§704.910-704.950. After a property settlement judgment, a spouse may not claim a homestead in the other spouse's property. *Wiltrakis v Wiltrakis* (1966) 244 CA2d 257, 53 CR 97.
- If property is held in joint tenancy and a joint tenant dies, the vesting of title in the survivor requires certain formalities, including recording an Affidavit of Death of Joint Tenant. See 1 California Decedent Estate Practice §§4.18-4.20 (Cal CEB 1986).
- If record title is held by someone who is deceased, the administrator or executor must usually obtain court approval of any conveyance. See 1 Decedent Estate Prac §§13.14-13.60.
- If the property is held in cotenancy by several people, all must execute the agreement and deed or execute powers of attorney in favor of the person executing those documents. All tenancy-in-common agreements should also be reviewed to confirm authority to sell the property.
- If the property is held in the name of a limited liability company, a certified copy of the articles of organization should have been recorded. See §4.27.
- If the property is held in the name of a general partnership, a Statement of Partnership Authority must have been filed with the Secretary of State and a certified copy should have been recorded. See §4.24. If it was held in a limited partnership, a Certificate of Limited Partnership (Form LP-1) or an Application for Registration, Foreign Limited Partnership (Form LP-5), showing the names of the current general partners, must have been filed with the Secretary of State. See §4.25.
- If the property is held in the name of a corporation, officers must be available who can sign the deed on behalf of the corporation. Some corporate formalities, *e.g.,* a directors' vote or a shareholders' vote, may have to be observed. See §4.28.
- If the property is held in the name of a trust, the trust document may have to be reviewed for any restrictions on transfers.

© The Regents of the University of California

D. Methods of Holding Title

§4.20 1. Entities

Most commercial real property is held by entities rather than by natural persons. Counsel for a buyer should consult with the client on the appropriate entity to hold title. If an existing business is to purchase the property, it is often appropriate for the existing entity to acquire the property (or a wholly owned subsidiary, if the existing entity is a corporation). If the property is to be held for investment, it is often appropriate to form a new entity.

When a new entity is to be formed and natural persons are the beneficial owners, many practitioners recommend that a limited liability company (LLC) be formed to hold title. An LLC combines the corporate characteristics of limited liability with the income tax characteristics of a partnership. In contrast to a limited partnership, there is no need to form and capitalize an entity to be the general partner. The unlimited liability of the partners of a general partnership is avoided, as is the double taxation inherent in a corporation taxed under Subchapter C of the Internal Revenue Code. The fee for an LLC doing business in California, however, is higher than for other entities. See Rev & T C §§17941-17943. A corporation taxed under Subchapter S of the Internal Revenue Code has limited liability and avoids double taxation, but will have greater maintenance expenses than does an LLC and will be subject to a 1.5-percent California income tax on its net income. Rev & T C §23802(b)(1). If the buyer intends to obtain conduit loan financing, the lender will frequently require that the borrowing entity be a single-purpose, bankruptcy-remote entity. On conduit loan requirements, see California Real Estate Finance Practice: Strategies and Forms §§1.90-1.107 (Cal CEB 2000).

For discussions of the choice of entity to hold real property, see generally Selecting & Forming Business Entities (2d ed Cal CEB 2007).

Counsel for the seller also needs to be aware of the type of entity holding title to the property and the title company's requirements for delivery of state-certified formation documents or other applicable authority documents such as tenancy-in-common agreements, operating agreements (for limited liability companies), trust agreements (for trusts), or bylaws (for corporations). Additionally, a nonindividual seller is generally required to provide a good standing certificate.

PRACTICE TIP: Although seller's counsel is advised to check the standing of the selling entity early in the sale process, many buyers require a state-certified good standing certificate dated no earlier than 5 business days before closing. Always check with the office of the Secretary of State to determine how quickly good standing certificates are being issued, taking into account peak sale periods such as the end of the year.

© The Regents of the University of California

§4.21 2. Community Property; Cotenancies; Separate Property

Rather than taking title in an entity (see §4.20), some clients wish to take title with their spouse (as community property), or with any other person or persons as tenants in common or joint tenants. See CC §682. The stated reason is usually simplicity and the desire to avoid the expense of forming a separate entity to hold title.

If buyers wish to take title as joint tenants or tenants in common, many practitioners recommend that the cotenants enter into an agreement spelling out their respective obligations to one another, specifying the method for managing the property, making decisions about it, and obligating themselves to contribute capital as needed. Without such an agreement, cotenants have limited obligations to contribute to the cotenancy other than as needed to preserve the property. See *Milian v DeLeon* (1986) 181 CA3d 1185, 1195, 226 CR 831 (in partition of joint tenancy, joint tenant who made larger contribution to downpayment not entitled to reimbursement in absence of agreement for reimbursement). Thus, if cotenants wish to require a periodic investment in the property or capital contributions for improvements, a written agreement must so state. It is also customary to waive or modify the right of partition in such agreements. For a form tenancy-in-common agreement, see App O. On cotenancies, see §§4.22-4.23. On severing joint tenancies, see Bernhardt, *Changing Course: Secretly Severing Joint Tenancies*, 19 CEB Real Prop L Rep 125 (May 1996).

A spouse's separate property is property acquired before marriage; property acquired by gift, bequest, devise, or descent; or property acquired with the profits or proceeds of such property. Fam C §770. The law presumes that property (other than separate property) acquired during marriage is community property (Fam C §§760, 2580-2581), regardless of whether ownership is characterized as joint tenancy or a tenancy in common. See *Marriage of Haines* (1995) 33 CA4th 277, 39 CR2d 673. The presumption can be overcome by a clear statement in the deed or other document that the property is separate property and not community property. Fam C §2581(a); *Marriage of Haines, supra*. Thus, when a husband or wife, or both, purchase property, the purchase agreement and the deed should specifically state whether the property is separate property or community property, regardless of how title is to be held. Likewise, a buyer of property from a married person or a married couple will want written evidence from both spouses as to the nature of the property, not merely the form of title by which the property is held.

After June 30, 2001, a husband and wife may hold title to property as "community property with right of survivorship." Thus, if the husband and wife intend that the deceased spouse's 50-percent interest in community property will automatically pass to the surviving spouse, title should expressly state the right of survivorship. CC §682.1(a); Fam C §750.

© The Regents of the University of California

E. Issues to Consider in Taking Title

1. Cotenancy

§4.22 a. Distinguishing Tenants in Common From Joint Tenants

There are two differences between a tenancy in common and a joint tenancy: First, tenants in common may have unequal undivided interests, but joint tenants' interests must be equal. CC §§683, 685. Second, on the death of a joint tenant, the surviving joint tenants take the entire interest, while the interest of a tenant in common forms part of his or her probate estate. See 12 Witkin, Summary of California Law, *Real Property* §§33-34 (10th ed 2005). Because of survivorship rights, a joint tenant's interest is not subject to testamentary disposition or, after death, to his or her debts. But see *Rupp v Kahn* (1966) 246 CA2d 188, 55 CR 108 (survivor's entire interest, resulting from conveyance by insolvent person without consideration, is subject to decedent's debts). A corporation may own land as a tenant in common. Under common law, a corporation cannot be a joint tenant with an individual or another corporation. In *American Bible Soc'y v Mortgage Guar. Co.* (1932) 217 C 9, 17 P2d 105, the court refused to decide whether common law still applied and held that the joint tenancy created a trust in favor of the charitable corporation named as a joint tenant in the gift deed.

TAX CONSIDERATIONS: A termination of joint tenancy results in a change of ownership for property tax purposes unless the proportionate interest of the joint tenants does not change as a result of the termination. 18 Cal Code Regs §462.040(b)(4). For a table listing events that trigger reappraisal, see App A.

© The Regents of the University of California

§4.23 b. Partition of Cotenancy

Of particular importance in cotenancies is an agreement that the entire property will be used to the mutual advantage of all and that none of the cotenants will partition the property (thus destroying the overall development or investment plan) without the others' consent. Although a cotenant's right to partition is absolute rather than discretionary with the courts, the right may be modified or waived in advance either expressly or by implication. *Penasquitos, Inc. v Holladay* (1972) 27 CA3d 356, 103 CR 717; *Thomas v Witte* (1963) 214 CA2d 322, 29 CR 412; *Asels v Asels* (1919) 43 CA 574, 185 P 419.

For further discussion of cotenancies, see Gutierrez, *Drafting and Reviewing Residential Cotenancy Ownership Agreements, Part 1*, 20 CEB Real Prop L Rep 153 (July 1997). For a form agreement among tenants in common, see App O. (This form provides in paragraph 17 that each cotenant retains the right to unilaterally seek to partition the property, but a cotenant must offer to sell his or her interest to the other cotenants before exercising that right.)

© The Regents of the University of California

§4.24 2. General Partnerships

Under the Uniform Partnership Act of 1994 (UPA) (Corp C §§16100-16962), which governs all general partnerships, a general partnership is viewed as a legal entity. Consequently, general partners are not co-owners of partnership property and have no transferable interest in such property. Corp C §16501. The partners' transferable interest is limited to their share of profits and losses and the right to receive distributions. See Advising California Partnerships §§14.17, 14.20 (3d ed Cal CEB 1999).

Any partner of a general partnership, or a general partner of a limited partnership, can bind the partnership or convey partnership property. Corp C §§16301-16302. Under UPA, the partnership is bound by acts performed in the ordinary course of partnership business unless the partner had no authority to act and the person with whom the partner was dealing knew or had notice that the partner was not authorized to act. Corp C §16302(b). If an act is performed that is not apparently in the ordinary course of the partnership business, it binds the partnership only if the partner was authorized to act. Corp C §16301(2).

Acquisition of partnership property is governed by Corp C §16204. The partnership's right to contract in the partnership's name concerning property is authorized by Corp C §16302. The usual form of providing notice of authority to act on the partnership's behalf is the Statement of Partnership Authority. Corp C §16303. The mandatory contents of the statement are in §16303. The statement may also specify the authority or limits on the general authority of some or all partners to enter into other transactions on the partnership's behalf in any other matter. Even if the filed statement does not contain all the mandatory information, it nevertheless operates with respect to a third person as if properly completed, as long as it states the partnership name and is executed appropriately. Corp C §16303(c). For a form Statement of Partnership Authority, see App F.

A grant of supplemental authority to transfer real property held in the name of the partnership and contained in a certified copy of a statement that has been filed and duly recorded is conclusive in favor of a person who gives value without contrary knowledge. Corp C §16303(d)(2). A person is considered to know of limitations on authority to transfer partnership real property if a certified copy of the statement containing the limitation is duly recorded. Corp C §16303(e). Authority for transfers of partnership real property not held in the partnership's name is governed by Corp C §§16301-16302.

On a title company's requirements for confirmation of the partners' authority to act, see California Title Insurance Practice §2.30 (2d ed Cal CEB 1997).

© The Regents of the University of California

§4.25 3. Limited Partnerships

Currently, California limited partnerships may be governed by different statutory frameworks, depending on when they were formed and what elections are made:

- Limited partnerships formed on or after July 1, 1984, but before January 1, 2008, are governed by the California Revised Limited Partnership Act (Revised Act) (Corp C §§15611-15724) (repealed operative Jan. 1, 2010).
- Limited partnerships formed before July 1, 1984, are governed by the California Uniform Limited Partnership Act (ULPA) (Corp C §§15501-15533), unless the partnership elects to be governed by the Revised Act. Corp C §15712(b)(1).
- Limited partnerships formed after January 1, 2008, are governed by the Uniform Limited Partnership Act of 2008 (2008 ULPA) (Corp C §§15900-15912.07); limited partnerships in existence before that date may elect to be governed by its provisions. Corp C §15912.06(a)(2).

NOTE: As of January 1, 2010, *all* California limited partnerships will be subject to the 2008 ULPA regardless of formation date.

Under the Revised Act, a limited partnership came into existence only when a Certificate of Limited Partnership (Form LP-1) was filed with the Secretary of State. See Corp C §15621. This process is essentially the same for limited partnerships formed after January 1, 2008; an LP-1 is still filed, but the form has changed. See Corp C §15902.01. A copy of the current version of the LP-1 may be obtained from the website of the California Secretary of State. See the Directory for details.

Recordation of the LP-1 creates a conclusive presumption in favor of any bona fide purchaser or encumbrancer of the partnership real property that the persons named as general partners in the certificate are the general partners of the partnership named and that they are all of the general partners of the limited partnership. Corp C §15621(d) (Corp C §15902.01(e), operative Jan. 1, 2008, for new or electing limited partnerships).

If an LP-1 is not filed, but a "Limited Partnership Agreement" is signed, the partners who signed as limited partners would probably be treated as joint venturers or general partners subject to personal liability unless they renounced their interest in the profits of the partnership and took advantage of the "escape clause" in Corp C §15633 (Corp C §15903.6, operative Jan. 1, 2008, for new or electing limited partnerships). See 9 Witkin, Summary of California Law, *Partnership* §§62, 69 (10th ed 2005).

For forms useful in drafting a limited partnership, see Advising California Partnerships, chap 19 (3d ed Cal CEB 1999).

© The Regents of the University of California

§4.26 4. Limited Liability Partnerships

Limited liability partnerships may be created under Corp C §§16951-16962 and may hold title to real property. Any domestic partnership, except a limited partnership, may convert to a limited liability partnership on a vote of the partners and by registering as such with the Secretary of State. On conversion to a registered limited liability partnership, real property of the former partnership is vested in the limited liability partnership. Corp C §16955. On converting a partnership to a limited liability partnership, see Advising California Partnerships §§3.12, 6.19, 12.27 (3d ed Cal CEB 1999).

© The Regents of the University of California

§4.27 5. Limited Liability Companies

The Beverly-Killea Limited Liability Company Act (Corp C §§17000-17654) created a new entity that has both corporate and partnership characteristics. A limited liability company (LLC) is taxed as a partnership for income tax purposes, but, like a corporation, it has limited liability. An LLC may consist of one or more members and comes into existence when articles of organization are filed with the California Secretary of State. Corp C §17050. The LLC's operation is governed by its operating agreement. The operating agreement need not be in writing. Certain provisions, however, such as indemnification of members, must be in writing to be effective; if the LLC is to be run by one or more managers and not by all its members, the articles of organization must so provide. Corp C §17151(b)-(c).

A certified copy of the articles of organization may be recorded. Recordation of the articles creates a conclusive presumption that the statements they contain are true and correct and can be relied on by bona fide purchasers and encumbrancers for value of the LLC's real property located in the county where the certified copy was recorded. Corp C §17052(f). On limited liability companies generally, see Forming and Operating California Limited Liability Companies (2d ed Cal CEB 2007). On converting to a limited liability company, see Limited Liab, chap 11.

For a form of a limited liability company certificate authorizing execution of documents required for the purchase of real property, see App E.

© The Regents of the University of California

§4.28 6. Corporations

If one party is a corporation, the other party must be assured that the corporation properly authorized the transaction. Corporations Code §313 provides that any conveyance signed by the chairman of the board, the president or any vice president, and the secretary, assistant secretary, chief financial officer, or any assistant treasurer of a California corporation, is not invalid for lack of authority, as long as the buyer did not have actual knowledge of the lack of authority.

NOTE: In *Snukal v Flightways Mfg., Inc.* (2000) 23 C4th 754, 759, 98 CR2d 1, the California Supreme Court concluded that under Corp C §313 "a contract is binding upon a corporation when an individual who in fact occupies the office of president, chief financial officer, *and* secretary of a corporation, executes a contract on behalf of the corporation, even when the contract expressly identifies the individual solely as its president."

Another way to establish that a sale of real property was authorized is for the corporate secretary to certify that the transaction was approved by the board of directors. The certification should state (Corp C §1002):

- That the property transferred is less than substantially all the corporation's assets;
- That the transfer is in the corporation's usual or regular course of business; or
- If the transfer is of substantially all the corporation's assets and is not in the corporation's usual and regular course of business, that the transaction has been approved by a majority of the outstanding shares as required by the Corporations Code.

For a form of corporate resolution authorizing execution of documents required for the purchase of real property, see App D.

A corporation comes into existence when its articles are filed with the Secretary of State. An inquiry to that office will ascertain whether a corporate party has filed its articles and is in good standing. Under Corp C §207(a), a corporate seal is no longer required to show corporate authority; thus, documents no longer need a corporate seal.

Agents of corporations entering into agreements that are made "subject to board of directors' approval" have a duty to act in good faith in seeking board approval, and the board must consider the proposal in good faith. *Jacobs v Freeman* (1980) 104 CA3d 177, 163 CR 680.

On a title company's requirements for confirming the corporation's authority to act, see California Title Insurance Practice, chap 2 (2d ed Cal CEB 1997).

© The Regents of the University of California

IV. INTRODUCTORY PROVISIONS OF AGREEMENT

§4.29 A. Preamble and Recitals

The preamble to the agreement should include the title of the agreement, its effective date, and the names of the seller and buyer. Often, each of these items is a defined term. It is customary to describe the type of entity for each party, such as a corporation or a limited liability company. If one party is an individual, it is customary to recite whether the individual is dealing in separate or community property. See preamble in form 4.167-1.

Many practitioners include factual recitals in the agreement. By giving the factual background to the transaction, recitals can aid in interpreting the agreement in a default. Recitals can be particularly helpful if the buyer intends to change the use of the property subject to obtaining permits or approvals, or if the seller is selling the property contingent on other transactions or approvals. See recitals in form 4.168-1.

© The Regents of the University of California

§4.30 B. Agreement to Buy and Sell

Two essential elements of a contract are the mutual consent of the parties and a sufficient consideration. It is thus customary to state the mutual agreement of the parties at the beginning of the agreement. See form 4.169-1. Agreements also often recite the receipt of consideration, but the recital would not be sufficient if, in fact, no consideration was given. On consideration, see §4.11.

© The Regents of the University of California

C. Description of Property

§4.31 1. Legal Description of Real Property

The legal description of the real property may be incorporated by reference, which avoids having a lengthy legal description in the body of the agreement.

PRACTICE TIP: Making the description an exhibit allows it to be prepared separately or photocopied from the seller's deed or a title insurance policy or preliminary report. This procedure saves time and reduces the chance of error in retyping the description. It is customary to include the assessor's parcel number.

If the property is not described by reference to a recorded subdivision map, the buyer should inquire with the city or county in which the property is located about its compliance with the Subdivision Map Act (Govt C §§66410-66499.37). Virtually every property division, even for leasing or financing, is regulated by that Act. See §4.92. On property descriptions, see chap 11.

© The Regents of the University of California

§4.32 2. Improvements and Appurtenances

The property description should describe the improvements being conveyed, including any street address, in order to avoid errors in description. It is customary to recite all other types of improvements on the property, although conveyance of the land includes conveyance of all improvements that are "affixed" to the land or are "fixtures" (CC §658; see *Southern Pac. Co. v County of Riverside* (1939) 35 CA2d 380, 95 P2d 688), unless the improvements have been severed.

It is also customary to describe all appurtenances to the land in order to avoid error. For example, counsel should ascertain whether the mineral rights are being conveyed with the property. Any appurtenant easements should be identified by legal description to ensure that they will be specifically conveyed by the grant deed and will be covered by the title insurance policy as insured parcels. On description of land, improvements, and appurtenances, see the recitals in form 4.168-1 and sections 1.2.1-1.2.3 of form 4.169-2.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.33 3. Personal Property

§4.33 3. Personal Property

Personal property that has not become a fixture does not pass to the buyer with the transfer of title to real property. The parties, however, may want to include personal property as part of the sale, and the agreement should specify which items of personal property are included. See section 1.2.4 of form 4.169-2.

PRACTICE TIP: If only a few items will be transferred, they can be listed in the agreement itself; otherwise, an inventory should be prepared and attached to the agreement as an exhibit.

When personal property is transferred, the buyer should be concerned about any liens on the personal property. The buyer achieves reasonable protection by obtaining from the seller a covenant of good title and a warranty that the property is free of encumbrances; the remedy is a claim against the seller for breach. A search of the Uniform Commercial Code Financing Statements filed with the Secretary of State (see Com C §§9302, 9401) will disclose any encumbrances of record, which the seller is then required to clear so that the warranty will be true at the closing.

PRACTICE TIP: The UCC search should be conducted as part of buyer's due diligence review, and should be updated as near to closing as possible.

If no major items of personal property are transferred and the buyer is confident that there are no encumbrances, the use of a warranty without a search may suffice. For a form bill of sale with warranties, see App H. For a discussion of security interests in personal property, see Secured Transactions in California Commercial Law Practice, chap 2 (2d ed Cal CEB 2001).

When substantial personal property is used in connection with normal business operations (as in a hotel), it is common to provide that the seller's warranty on that property is subject to dispositions, replacements, and acquisitions in the normal course of business.

PRACTICE TIP: If the seller is to take back a note secured by the real property and the personal property (*i.e.,* "mixed collateral"), the seller's attorney should carefully consider the effects of the one-form-of-action rule (CCP §726) and the antideficiency rule (CCP §580b) and advise the seller on those rules. See California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 9 (4th ed Cal CEB 2009).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.34 4. Intangible Property

§4.34 4. Intangible Property

The buyer should also identify whether other items, in addition to the real property (including improvements) and personal property (see §§4.32-4.33), should be included in the description of the property to be conveyed under the agreement, such as leasehold rights, contract rights, plans and specifications, permits, and licenses. If the building is new or if improvements were recently added to the property, warranties may exist that could be assignable to the buyer. Any rights may have considerable value, and buyers usually want a specific assignment of them. Various types of commercial property will also have intellectual property associated with the property, such as trademarks, tradenames, service marks, and telephone numbers. These should also be included in the description. See section 1.2.4 of form 4.169-2. For a form assignment of intangibles, see App J.

© The Regents of the University of California

V. PURCHASE PRICE AND DEPOSIT

A. Price

§4.35 1. Type of Consideration

The agreement should clearly and completely define the consideration to be delivered by each party and the method of payment, including amounts paid outside of escrow, amounts paid through escrow, and the terms of any notes, to the extent those terms are known. See form 4.170-1—4.170-5.

Under Ins C §12413.1, all title companies and escrow companies controlled by title companies must have good funds (*i.e.*, available for withdrawal) in their possession before closing. Wire transfers are the only method of providing immediate credit and are thus widely used. Cashier's, certified, or teller's checks are not available for disbursement until the business day following the business day of deposit. 12 CFR §229.10.

When the price is by unit, *e.g.,* per acre, it is essential that the total number of units be verified. Because a surveyor cannot certify to the precise number of acres or other units, the degree of certainty should be specified, *e.g.,* to the nearest 1/1000 of an acre. On the need for a survey and matters to consider in determining gross or net area, see §§4.58-4.59, 11.16.

The buyer may wish to pay only for usable land. If the purchase price is stated at a rate per acre of "usable land" or rate per "net acre," misunderstandings are likely to arise unless these terms are defined.

PRACTICE TIP: If the buyer cannot establish how much of the land can be used and its value to him or her, the agreement should include an explicit definition of what constitutes "usable land" or "net acres," by description, by contour or contour changes, or by excluding portions of the property such as those that are or may be dedicated for streets.

A frequently used alternative is to compute the purchase price based on the development density eventually approved for the property by applicable governmental agencies.

EXAMPLE: If the property is to be developed with apartments, the purchase price might be based on the number of units per acre permitted for development. The seller may establish a minimum price and require the buyer to apply for governmental approvals permitting development with a specified number of units per acre.

© The Regents of the University of California

§4.36 2. Allocation of Purchase Price

For income tax purposes, the buyer and seller must allocate the purchase price to the various types of assets being transferred, and may wish to document that allocation in the sales agreement. The asset types typically found in a real property transaction are land, real property improvements, tangible personal property, and (occasionally) intangible personal property. The differentiation among asset types occurs because land is not depreciable for income tax purposes and the cost recovery methods differ among real property and various types of personal property. The allocation could affect the seller's total tax liability, particularly if the improvements have been fully depreciated and the seller's cost basis for the land is a significant fraction of the purchase price. The buyer may have a conflicting interest, wishing to allocate more of the purchase price to depreciable improvements and personal property and less to land than the seller would prefer. The buyer's allocation may affect the amount of its taxable gain on a subsequent disposition of the property. The buyer will also need to allocate the purchase price among land, real property improvements, and personal property for California property tax purposes.

In ascertaining the income tax rules for allocation of a purchase price among several assets being sold, the parties must first determine whether the assets have been used by the seller or will be used by the buyer in the conduct of a trade or business. If so, the general provision regarding sales of capital assets under IRC §1221 does not apply and the parties must follow the detailed allocation rules set out in IRC §1060. There is no definition in the Internal Revenue Code or its regulations of what activities constitute a trade or business for these purposes. Some cases have held that ownership of a single rental property constitutes a trade or business. See generally Rothman, *Capital Assets*, 561 Tax Mgmt Portfolio, p A-66 (2001).

If the property is used in a trade or business, the consideration must be allocated first to cash and then to other assets in the order specified in §1060. The consideration allocated to an asset is limited to its fair market value. Any portion of the purchase price in excess of the fair market value of tangible and intangible assets must be allocated to good will (which would be unusual in a real estate transaction). If the parties agree in writing on an allocation of the purchase price, the allocation is generally binding on both the buyer and seller. IRC §1060(a)(2). If the parties do not allocate the purchase price in a written agreement, they still must report the allocation to the Internal Revenue Service on IRS Form 8594 for acquisitions after March 15, 2001. Treas Reg §1.1060-1(e)(1)(ii). See Rothman, p A-103. California's income tax law conforms to the federal law regarding allocation of the purchase price for a trade or business.

If the property is held for the production of income but is not used in a trade or business, as is the case for many parcels of real property, the parties must allocate the purchase price so that the seller may calculate gain or loss and the buyer may calculate the depreciable basis for real property improvements and personal property. In general, the allocation must be in proportion to the fair market value of each asset. See Maule, *Taxation of Real Estate Transactions—An Overview*, 590 Tax Mgmt Portfolio, p A-138 (2000).

In the authors' experience, few California real property sale agreements have provided for allocation of the purchase price, probably because the interests of the buyer and seller conflicted and the parties could not agree on an allocation. That practice may change for real property used in a trade or business, given the new requirement to file IRS Form 8594. For a form provision allocating the purchase price, see form 4.170-6. For an allocation of purchase price form, see §4.182.

© The Regents of the University of California

§4.37 B. Deposit

The purpose of the deposit is to demonstrate the buyer's good faith and to provide a fund from which the seller's damages may be recovered. (The latter may be of little immediate help to the seller, however, because escrow holders are generally unwilling to release funds without authorization from the parties after the alleged breach.) The nature and amount of the deposit is for the parties to decide, subject to the restrictions on liquidated damages (discussed in §4.142). Usually, the amount of the liquidated damages is equal to the deposit. The deposit should at least cover all escrow charges and generally be large enough to cause a buyer who may later contemplate backing out considerable discomfort at the prospect of having funds tied up for a long time.

Deposits usually consist of cash, but they may consist of documents readily convertible to cash, such as the assignment of a savings account or a letter of credit with instructions to the escrow holder to draw against it in specified circumstances. A letter of credit often presents problems because it typically expires within a specific period (usually 1 year or less). To ensure that the funds are available if a dispute occurs, the escrow holder must be authorized to draw on the letter of credit before it expires. See section 2.2.4 of form 4.170-2.

Deposit checks should be made payable to the escrow holder, who will hold the funds in trust. It is rarely advisable to make a deposit check payable to the seller, because the seller may cash it before accepting the offer or the broker may deliver it to the seller prematurely. Also, the escrow holder usually requires that funds be deposited into escrow before the escrow opens. If the escrow is canceled, the escrow holder looks to these funds for its cancellation charges.

The parties should instruct the escrow holder to place the deposit in an interest-bearing account and designate which party is to be credited with the interest, unless the size of the deposit and the length of the escrow are such that the return would be insignificant. If cash passes outside of escrow, this fact should be stated in the agreement, including a statement on whether the cash applies against the purchase price and, if the transaction fails, who receives the funds.

On cancellation of escrow, see §15.97; for form escrow cancellation instructions, see App S.

© The Regents of the University of California

C. Purchasing Subject to Existing Encumbrances

§4.38 1. Credit to Purchase Price

A buyer who acquires real property subject to an encumbrance usually receives a credit against the purchase price in an amount equal to the unpaid principal balance of the secured obligation, plus the accrued interest on the obligation prorated through the date of close of escrow. Taking title subject to an existing encumbrance may permit the buyer and the seller to avoid prepayment penalties and refinancing costs and to retain an existing encumbrance with a favorable interest rate. The terms of the underlying deed of trust and the interest rate on the secured promissory note should be examined by the buyer and compared with those available with new financing. The agreement should also allocate liability between the parties for any other lender charges and should provide for transferring any impound account balances to the buyer with a statement that the seller gets a credit for the sums transferred.

© The Regents of the University of California

2. Review of Loan Documents

§4.39 a. In General

If any existing deed of trust will not be removed of record, the buyer, for its protection, must have an opportunity to examine both the promissory note and the deed of trust securing it. If the agreement merely provides that the buyer takes subject to or assumes the existing note and deed of trust, the buyer has no opportunity to approve them. For example:

- The lender may have the right to accelerate the loan's maturity date on a sale of the property or on the buyer's violation of a covenant;
- Prepayment may not be permitted, or the prepayment penalty may be too costly;
- Destruction of existing improvements or removal of trees and vegetation may be prohibited or result in acceleration;
- There may be restrictions on use;
- The borrower may be obligated to make improvements;
- Release provisions may be nonexistent or unrealistic; or
- The deed of trust may cover additional real property, exposing the buyer to acceleration or foreclosure for a breach over which the buyer has no control.

The buyer should require the lender to provide a beneficiary statement under CC §2943. Such a statement may serve several purposes:

- Because it is signed by the lender (the mortgagee or the beneficiary), a statement may estop the lender from asserting a different balance later;
- Because the last payment date is given, a statement may furnish a clue to possible existing defaults;
- If the creditor has a right to object to the sale, its consent is essential; and
- If the buyer intends to leave any encumbrance in existence, the creditor's insistence that the buyer assume the debt rather than take subject to it (see §§4.41-4.42) may be crucial to the transaction.

On beneficiary statements, see California Title Insurance Practice, chap 2 (2d ed Cal CEB 1997).

© The Regents of the University of California

§4.40 b. Issues in Securitized Loans

Loans secured by income properties are often pooled together and then transferred to an entity, created for that purpose, which then funds the loans by selling securities. Principal and interest paid on the pooled mortgage loans are used to repay the securities. These securities often are rated by rating agencies (such as Standard & Poor's or Moody's Investors Service) based on the credit-worthiness of both the borrowers on the underlying mortgage loans and the tenants of the commercial properties, and similar factors. The mortgage loans are managed by a company hired for that purpose, often referred to as the "servicer." On securitized loans generally, see California Real Estate Finance Practice: Strategies and Forms, chap 1 (Cal CEB 2000).

Typically, securitized loan documents will

- require the borrower to obtain all necessary consents from the servicer and any other parties (as specified in the loan documents) before the borrower transfers the property;
- require the borrower to pay an assumption fee and the servicer's expenses;
- limit changes in the use of the property;
- require the buyer's credit to be at least as good as that of the seller;
- prohibit prepayment for part or all of the term of the loan; and
- require consent of the rating agency if the securities issued were rated.

Thus, counsel for both the seller and the buyer should carefully review the terms of securitized loan documents and any applicable rating agency requirements to ascertain whether the buyer will be qualified to assume the loan, the steps required during due diligence, and the time required to obtain consent to the loan assumption. Specifically, counsel should be aware of the following:

- The standards set for loan assumption;
- The consents required; and
- The delays often encountered in meeting these standards and obtaining these consents.

© The Regents of the University of California

3. Buyer's Personal Liability

§4.41 a. Assuming Encumbrances

Except when the note or deed of trust contains a due-on-sale clause (discussed in §4.43), the buyer may assume a loan through a written agreement with either the lender or the seller. If the latter, a recital in the deed constitutes a sufficient writing (CC §1624(a)(6)), and the assuming buyer becomes personally liable to the beneficiary for repayment of the loan under a theory of equitable subrogation (*Braun v Crew* (1920) 183 C 728, 192 P 531). Assumption of the debt does not release the seller from liability, but the seller's liability becomes that of a surety. *Everts v Matteson* (1942) 21 C2d 437, 132 P2d 476; *Birkhofer v Krumm* (1935) 4 CA2d 43, 40 P2d 553. Generally, the suretyship principles of law apply. See *Woodward v Brown* (1897) 119 C 283, 51 P 542 (effect of release of part of encumbered property); *Wise v Clapper* (1968) 257 CA2d 770, 65 CR 231 (extension of time for payments). A seller who incurs liability for a deficiency may seek indemnification from the assuming grantee. *White v Schader* (1921) 185 C 606, 198 P 19; *Robson v O'Toole* (1919) 45 CA 63, 187 P 110.

These rules are modified if the original loan comes under the antideficiency provisions of CCP §580b. See generally California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 9 (4th ed Cal CEB 2009). If the loan was initially a purchase money loan under §580b, the assuming grantee will be entitled to the antideficiency protection of that statute, whether the original loan was made by the vendor (*Jackson v Taylor* (1969) 272 CA2d 1, 76 CR 891 (see also *Cornelison v Kornbluth* (1975) 15 C3d 590, 125 CR 557)) or a third party (*Kistler v Vasi* (1969) 71 C2d 261, 78 CR 170). If the original secured obligation was not a purchase money loan, the grantee will not be entitled to §580b protection if the obligation is assumed under circumstances that would make a new loan not a purchase money loan (*Brown v Jenson* (1953) 41 C2d 193, 259 P2d 425), which is probably also true even if a new loan to the buyer would come under §580b (*Jackson v Taylor, supra*; see Mortgage & Deed of Trust §9.128).

The agreement should indicate whether the buyer or the seller will pay any loan assumption fee charged by the lender. See form 4.170-3 for loan assumption language; see section 7.8.5 of form 4.175-8 for a provision allocating assumption fees to seller.

© The Regents of the University of California

§4.42 b. Taking Subject to Encumbrance

A buyer who merely takes subject to an existing encumbrance is not burdened with personal liability for the underlying obligation (*Cornelison v Kornbluth* (1975) 15 C3d 590, 125 CR 557), but the property remains as security for payment of the obligation. Subject to the effect of CCP §580b, the maker or guarantor of the note, or the person who had previously assumed liability, remains liable (see *Ward v De Oca* (1898) 120 C 102, 52 P 130); if that person subsequently pays the liability, he or she acquires no rights against the buyer but is subrogated to the mortgagee's right to foreclose against the property (*Vincent v Garland* (1936) 14 CA2d 725, 58 P2d 1320). See also CC §§2848-2849; *Sanders v Magill* (1937) 9 C2d 145, 70 P2d 159; Rintala, *California's Anti-Deficiency Legislation and Suretyship Law: The Transversion of Protective Statutory Schemes*, 17 UCLA L Rev 245, 284 n116 (1969). A nonassuming buyer, however, will be personally liable for bad faith waste and, in the absence of a CCP §580b or §580d defense, for waste resulting from negligent conduct. *Cornelison v Kornbluth, supra*; Leipziger, *The Mortgagee's Remedies for Waste*, 64 Cal L Rev 1086, 1129 (1976).

© The Regents of the University of California

§4.43 4. Due-on-Sale Provision

A due-on-sale provision in the existing note and deed of trust restricts the new buyer's ability to take subject to or to assume the existing obligation. A due-on-sale provision permits the secured lender to accelerate the loan in a sale or other specified transfer or transaction affecting the property. See California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 8 (4th ed Cal CEB 2009). Enforcement of due-on-sale provisions is governed by the Garn-St. Germain Depository Institutions Act of 1982 (Garn Act) (12 USC §1701j-3), which preempts all state law, including judicial decisions, limiting or restricting enforcement of due-on-sale provisions in real property loans. Under the Garn Act, enforcement of these provisions is governed exclusively by the loan contract. Garn Act §341(b)(1) (12 USC §1701j-3(b)(1)). For further discussion of the Garn Act, see §§9.50-9.52.

© The Regents of the University of California

§4.44 D. Seller Financing

When the buyer is to take subject to or is to assume an existing encumbrance, information sufficient to identify the loan is all that need be recited. When the seller is to provide financing, however, a fuller description must be given so that no further negotiations are necessary on the terms of the loan.

If possible, the forms of the note and deed of trust should be attached as exhibits. If this is not done, the agreement should specify their essential terms, *i.e.,* interest rate, principal sum, maturity date, and number and amount of installment payments, and should state whether any special provisions, *i.e.,* late charges, prepayment restrictions, or due-on-sale provisions, are to be included. See chap 9 for a complete discussion of seller financing. See form 4.170-4.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.45 VI. DUE DILIGENCE

§4.45 VI. DUE DILIGENCE

Whether acquiring raw land for development or property improved with existing residential or commercial buildings, buyers need assurance that the property is suitable for the buyer's intended purpose. Buyers also need to know the property's condition and state of repair (or disrepair). A buyer's review of the physical aspects of the property and the various factors that affect its use and value is commonly known as "due diligence."

The importance of a buyer's careful investigation of the property cannot be overstated. Buyers are advised not to rely too much on the representations and warranties in the purchase contract, but to treat the purchase as if it were an unqualified "as-is" purchase. Litigating defects or misrepresentations after closing is rarely a satisfactory substitute for a well-conducted, thorough due diligence investigation. For a buyer's commercial property due diligence checklist, see App B. For a checklist of due diligence materials to be delivered by the seller in a commercial property sale, see App C.

PRACTICE TIP: If the attorney for the buyer takes an active role in completing the due diligence or analyzing information provided by consultants, then the attorney may be liable for any losses the buyer suffers by virtue of purchasing the property without the benefit of material facts known or discovered by the attorney, but not disclosed to the buyer. See, *e.g., Keywell Corp. v Piper & Marbury, LLP* (WD NY, Feb. 11, 1999, No. 96-CV-0660E) 1999 WL 66700, 1999 US Dist Lexis 1445 (attorneys who directed environmental consultants to limit their investigation and failed to disclose to their client the consultants' concerns about the limited nature of their review could be liable for lost profits from unexpectedly high clean-up costs). Thus, the attorney should obtain client approval of the scope of due diligence, provide full copies of all reports related to the property, highlight all material facts, and encourage the client to separately review such reports.

© The Regents of the University of California

§4.46 A. Methods of Providing for Due Diligence

The buyer needs time in which to conduct its due diligence investigation. It is common practice to sign a written agreement allowing the buyer to undertake due diligence and to withdraw from the transaction if the property does not meet the buyer's needs. There are a number of ways to arrange this investigation. The most common method is for the parties to sign a purchase agreement that is subject to conditions precedent, warranties, covenants, or combinations of these devices. The agreement is consummated if the conditions are met, the warranties prove true, and the covenants are performed. If not, the party for whose protection the provision was inserted may withdraw from the agreement or seek damages against the other party. The buyer may also be able to obtain specific performance at a reduced purchase price. The exact nature of the remedy depends on the kind of protection written into the purchase agreement.

Another option, which is becoming more widely used in commercial transactions between sophisticated parties, is to allow the buyer to begin conducting its due diligence before the execution of the purchase agreement, but after execution of a letter of intent. For a discussion of letters of intent, see chap 3. In such circumstances, a separate access and indemnity agreement is signed between the parties, the indemnity provisions of which remain binding even if the buyer elects not to proceed with the transaction. For a sample access license and indemnity agreement, see App P. A third alternative is for the parties to enter into an option agreement. For a discussion of option agreements, see chap 8.

© The Regents of the University of California

B. Due Diligence Conditions

§4.47 1. Purpose of Due Diligence Conditions

Virtually all sales agreements for California real property contain at least one provision conditioning the buyer's obligation to perform on the occurrence or nonoccurrence of some event, the existence or nonexistence of some fact, or on someone's approval or disapproval of something. Commonly called "conditions," "contingencies," or "out" clauses, they allow the buyer to execute an agreement promptly and to withdraw from the transaction if the condition is not met. Typical of such conditions are those requiring the following:

- The approval of a third party, *e.g.,* a planning commission or a lending institution;
- The buyer's satisfaction with the economic performance of the property;
- The buyer's satisfaction with physical conditions that are discoverable only after time-consuming tests, *e.g.,* soil tests or engineering studies (see §§4.77-4.80); and
- The buyer's satisfaction with the condition of title, such as the terms of deeds of trust, leases, or covenants, conditions, and restrictions.

If the execution of an agreement were to be postponed until the buyer could properly check all the conditions, either the seller's property would have to be kept off the market without any commitment from the buyer or the buyer would have to spend time and money checking out property that might be sold to another at any time. An option can often solve these problems as effectively as can conditional agreements. On options, see chap 8. The advantage to the buyer of a conditional sales agreement lies in the return of the deposit if the condition fails. See §4.3 for a discussion of conditional contracts and the application of the implied covenant of good faith to a buyer's approval of due diligence conditions.

© The Regents of the University of California

§4.48 2. Drafting Considerations

Conditional sales agreements typically provide the buyer a period of time within which to conduct its due diligence and require the seller to make the property and the seller's documents regarding the property available for the buyer's inspection during the due diligence (or "contingency") period. The length of the due diligence period will vary according to the type of property and the nature and extent of consents that must be obtained (such as development approval from the appropriate city or county or consent from a lender). Sellers typically negotiate for a shorter due diligence period (15 or 30 days) and buyers seek a longer one (60 or 90 days, or longer).

Each party will use various drafting techniques to improve its position. For example, a buyer's tactic is to delay the start of the due diligence period until "all documents" regarding the property have been delivered to the buyer. A buyer also will want the right to approve or disapprove a condition in its sole discretion. For a discussion of the buyer's obligation to undertake its investigation in good faith, see §4.3. A seller's tactics may include the following:

- Starting the due diligence period immediately on execution of the sales agreement;
- Limiting the number of documents the seller must deliver to the buyer; and
- Requiring the buyer to inspect other documents at the seller's office (or at the office of seller's counsel).

Compare Alternatives 1 and 2 in section 3.1 of form 4.171-1. Alternative 2, favoring the seller, limits the documents the seller must deliver to a preliminary report on title, a rent roll, tenant leases, and recent operating statements.

Sellers of commercial property will generally require a buyer and its consultants to carry specified amounts of liability insurance naming seller as an additional insured, and to provide proof of such insurance before commencement of any on-site inspections or testing. For a discussion of liability insurance, see chap 14. Sellers will also seek to obtain an indemnity agreement from the buyer for any property damage caused by buyer's testing and require that the buyer restore the property to its pre-testing condition. For provisions, see section 3.5.2 of form 4.171-5.

Counsel should also specify what happens at the end of the due diligence period, often referred to as the "contingency date." The agreement should specify whether inaction by the buyer will terminate the agreement or operate as a waiver of all the buyer's conditions. The agreement should also provide for return of the deposit to the buyer if the buyer terminates the agreement. See the discussion in §§4.99-4.100.

© The Regents of the University of California

§4.49 C. Seller's Disclosure Obligations

The seller is obligated to inform the buyer of any facts materially affecting the value or desirability of the property that would not be apparent to the buyer on inspection. *Lingsch v Savage* (1963) 213 CA2d 729, 29 CR 201. Whether a defect is discoverable on inspection is often a difficult question of fact. Because the seller is usually in the best position to know the condition of the property, the buyer may insist that the seller disclose the defects in the property, whether apparent or not, and give a warranty against any defects other than those disclosed. The older the improvements on the property, however, the more likely it is that defects do exist, and the seller may insist that the buyer make its own inspection and purchase the property "as is" in reliance on that inspection. Even an "as is" provision does not relieve the seller of the obligation to disclose material defects of which the seller is aware. *Lingsch v Savage, supra*. See §4.120 for discussion of "as is" provisions.

Sellers have a variety of statutory disclosure obligations. For example, under CC §1102.18, sellers must disclose any known release of an "illegal controlled substance" on the property. See §§6.6-6.29 for discussion of a variety of disclosure requirements for one-to-four-unit residential properties. Sellers of nonresidential property must make disclosures concerning any known hazardous substance on the property. Health & S C §25359.7. See the discussion of this requirement in §4.80. The Toxic Mold Protection Act of 2001 (Health & S C §§26100-26156) requires sellers of commercial and industrial properties to disclose to buyers the presence of mold in the property known to the seller if the mold exceeds exposure limits to be established by the Department of Health Services. Health & S C §26140. The disclosure requirement will become effective only after the department adopts standards and guidelines under the Act. Commencing January 1, 2010, a nonresidential building owner or operator must disclose to prospective purchasers the Energy Star Portfolio Manager benchmarking data and ratings for the most recent 12-month period. Pub Res C §25402.10(d). For more information on the Energy Star Program, see the EPA website at the URL in the Directory. For a list of other necessary disclosures, see §1.64. For a discussion of required residential disclosures, see chap 6.

PRACTICE TIP: It is often helpful for a seller to gather its due diligence and disclosure materials before marketing the property and approach the sale as if it were a fully warranted transaction, even when it is not. The result is thoughtful and careful pre-sale due diligence by the seller to ensure that the disclosures are complete, accurate, and made early in the transaction—when they are the least harmful to the seller's negotiating position. Even though most sellers may readily understand the concept of fraud, they may find it more difficult to understand related concepts such as negligent misrepresentation and mistake, especially when these concepts compete with a desire to cultivate the buyer's interest in the property. Counsel for the seller should thoroughly review the disclosure requirements with the client.

A seller's breach of duty to disclose material facts to the buyer may result in liability to subsequent buyers if the seller has reason to expect the misrepresentations will reach subsequent buyers. In *Geernaert v Mitchell* (1995) 31 CA4th 601, 37 CR2d 483, home buyers were permitted to sue a previous owner of the property for alleged fraudulent misrepresentations the predecessor made to their seller. The court held that if the defendant had reason to expect that the misrepresentations would be repeated and acted on by a third person (the current buyers), the defendant could be liable to that third person.

For discussion of a buyer's remedies for a seller's failure to disclose known material facts, see California Real Property Remedies and Damages, chap 3 (2d ed Cal CEB 2002).

© The Regents of the University of California

D. Title

1. Marketable Title

§4.50 a. Definitions of Marketable Title

Under California law, a buyer of real property is entitled to "marketable title" as an implied condition of the bargain. *King v Stanley* (1948) 32 C2d 584, 197 P2d 321. Marketable title must "embrace both the legal and equitable estates, must be free from any encumbrance, [and] must be defensible and salable." *Palos Verdes Corp. v Housing Auth.* (1962) 202 CA2d 827, 838, 21 CR 225. Title must be sufficiently free from doubt that a reasonable buyer, well informed about the facts and their legal effect and exercising ordinary business prudence, would be willing to accept it. *Hocking v Title Ins. & Trust Co.* (1951) 37 C2d 644, 234 P2d 625; *Wilson v Pacific Coast Title Ins. Co.* (1951) 106 CA2d 599, 602, 235 P2d 431. The general rule is that restrictions imposed by law, such as local zoning ordinances, do not impair marketability, because the parties are considered to have contracted in light of applicable law. *Hartman v Rizzuto* (1954) 123 CA2d 186, 266 P2d 539. A visible encumbrance, such as a road, is not considered to render title unmarketable, because the parties are considered to have contracted with the encumbrance in mind. *Evans v Faught* (1965) 231 CA2d 698, 42 CR 133.

© The Regents of the University of California

§4.51 b. Examples of Unmarketable Title

In general, matters affecting title that are not visible, but are prejudicial, will render title unmarketable. Examples of such defects include:

- Easements of record unless they are visible;
- Judgment liens;
- Deeds of trust and mortgages;
- Covenants, conditions, and restrictions or similar restrictive covenants affecting the property;
- Tax and assessment liens;
- Mechanics' liens;
- Adverse possession; and
- Leases.

On unmarketability of title, see California Title Insurance Practice, chaps 6-7 (2d ed Cal CEB 1997). On discussion of encumbrances that render title unmarketable, see 1 Miller & Starr, California Real Estate §2:23 (3d ed 2000).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.52 c. Statutory Procedures for Curing Certain Title Defects

§4.52 c. Statutory Procedures for Curing Certain Title Defects

The Civil Code provides specific procedures to cure title defects caused by ancient or expired interests in property:

- CC §§882.020-882.040 cover the expiration of ancient mortgages and deeds of trust;
- CC §§885.010-885.070 cover the expiration of powers to enforce conditions subsequent;
- CC §§886.010-886.050 cover the expiration of unperformed contracts for sale of real property; and
- CC §§880.020-880.370 (on marketable record title) simplify and facilitate the transfer of real property in which interests or defects in title were created in remote times and are no longer valid.

See §8.21 for discussion of expiration of unexercised options.

© The Regents of the University of California

§4.53 2. Title Insurance

Title insurance has become the customary way to protect a buyer against defects in title. Although a title insurance policy does not remove a defect in title (*Frabotta v Alencastre* (1960) 182 CA2d 679, 6 CR 536), it provides the buyer with a means of recovery of loss or damages if title proves to be unmarketable. Special endorsements are available from title companies to solve some of the more common title problems. The buyer may also be able to negotiate with the title company to eliminate an exception from the policy. Eliminating an exception may not be a permanent solution, however, because there is still the risk that a subsequent buyer might not be able to obtain the same policy coverage. See California Title Insurance Practice (2d ed Cal CEB 1997) for a detailed discussion of title insurance.

PRACTICE TIP: The American Land Title Association (ALTA) has adopted a new title insurance policy and endorsement forms, effective June 17, 2006. See California Title Insurance Practice, chap 6 (2d ed Cal CEB 1997) for a discussion of the ALTA policy and endorsement forms. There is no implied obligation of the seller to furnish title insurance (see *Easton v Montgomery* (1891) 90 C 307, 27 P 280; *Seymour v Shaeffer* (1947) 82 CA2d 823, 187 P2d 95, disapproved on other grounds in *Ellis v Mihelis* (1963) 60 C2d 206, 216, 32 CR 415); the agreement should expressly provide for it. On available policies and endorsements, see Title Ins, chaps 6-7. The amount of coverage is usually the purchase price of the property, though this may vary. In the Bay Area and some other Northern California counties, the buyer generally pays for title insurance. In many Central Valley and northeastern counties, the title insurance cost is split. In Southern California, custom calls for the seller to pay this charge. See §§15.7-15.15, 15.40.

If no title policy will be issued, other title company products are available that provide some information regarding the property. For a discussion of such products, see California Title Insurance Practice, chap 9 (2d ed Cal CEB 1997).

© The Regents of the University of California

a. Preliminary Report

§4.54 (1) Contents of Preliminary Report

It is standard procedure for the buyer to obtain a preliminary report that summarizes the exceptions to marketable title that the title company has found. Generally, the seller has a certain period of time to obtain the title report following the execution of the purchase agreement, although sophisticated commercial sellers will order the title report before marketing the property. A preliminary report contains a description of the property and encumbrances of record, with a map, which may simply be a copy of the applicable assessor's parcel map or may be a subdivision map showing the surveyed property boundaries. Title companies usually summarize, by reference to recorded documents, the general nature of the items affecting title, such as easements, covenants, conditions, and restrictions, equitable servitudes, monetary liens (such as taxes and deeds of trust), leases, or lis pendens. See §§4.60-4.69. These items will be listed as "exceptions" to coverage in the title policy obtained for the property. To fully understand the nature and extent of these exceptions, the underlying documents must be ordered from the title company and analyzed. Buyer's counsel should review the assembled information with the client to determine whether the property, so impaired, is acceptable or unacceptable.

On obtaining and reviewing the preliminary report, see California Title Insurance Practice, chaps 2-3 (2d ed Cal CEB 1997). On contents of the preliminary report, see Title Ins, chap 5.

PRACTICE TIP: Before marketing the property and executing a purchase agreement, seller may wish to obtain a preliminary report and copies of all title exceptions to determine if there are any title problems that might adversely affect the sale of the property.

© The Regents of the University of California

§4.55 (2) Nature of Preliminary Report

In dealing with preliminary reports, the lawyer should keep three key points in mind:

- A preliminary report is not a legal title document, but merely a report of certain information concerning title. There may well be unrecorded matters affecting title that do not appear in the report, and, because mistakes can happen, there may even be recorded matters that the title company has failed to include in the report. On unrecorded defects in title that do not appear on a preliminary report, see §§11.10, 11.78-11.88. See also California Title Insurance Practice, chap 5 (2d ed Cal CEB 1997).
- The map attached to the preliminary report does not assure the client that the property described in the report is exactly the same as the property the client wishes to purchase or sell. For that information (and other information), the client will need to refer to a current survey or have a survey conducted. See §1.100; Title Ins §5.7.
- A preliminary report is not an insurance policy, and cannot be relied on as a representation of the condition of title to the property. For reports issued before January 1, 1982, the California Supreme Court held title companies accountable for the accuracy of such reports based on a negligence standard of care. See *White v Western Title Ins. Co.* (1985) 40 C3d 870, 221 CR 509; *Lawrence v Chicago Title Ins. Co.* (1987) 192 CA3d 70, 237 CR 264. Effective January 1, 1982, a preliminary report may not be construed as a representation as to the condition of title to real property, but rather as a statement of the terms and conditions on which the title company is willing to issue its title policy if the offer is accepted. Ins C §12340.11. See also *Fidelity Nat'l Title Ins. Co. v Miller* (1989) 215 CA3d 1163, 264 CR 17. Thus, the lawyer should regard the preliminary report as an essential tool in the client's investigation of the condition of title, not as a complete or assured account of that condition. For further discussion, see Title Ins §§5.25-5.29.

Because title companies do not ensure the accuracy of their preliminary reports (in contrast to title insurance policies), counsel should discuss any possible unlisted exceptions to title with the title officer to avoid last-minute difficulties. The preliminary report may include exceptions that can be eliminated, such as expired leases or liens that have been paid. Counsel should investigate each exception and discuss with the title officer any that can be eliminated. On preliminary reports, see Title Ins, chap 5.

PRACTICE TIP: Buyer's counsel should look beyond marketability of title, because the courts have held that some matters that affect the use of the property do not impair title even when they reduce the property's value. For example, in *Nishiyama v Safeco Title Ins. Co.* (1978) 85 CA3d Supp 1, 149 CR 355, the court held that the facts that the property had been divided in violation of the Subdivision Map Act, and that the owner might be required to comply with conditions that could have been imposed had the property been subdivided in compliance with the law, did not render title unmarketable. See also *Hocking v Title Ins. & Trust Co.* (1951) 37 C2d 644, 234 P2d 625. For further discussion of marketability, see Title Ins, chaps 6-7, 11. See discussion of visible easements in §4.64.

© The Regents of the University of California

§4.56 (3) Fees and Costs

There is generally no charge for a preliminary report unless a title policy is not issued. The fee varies from company to company and from time to time. Fees in the range of $200 to $500 are typical. The lawyer should make sure that the client is aware of this potential expense, provide any assistance the client may need in obtaining specific cost quotes for the title report, and confirm that the client is prepared to incur that expense. On premiums for title policies and methods of reducing same, see California Title Insurance Practice, chap 3 (2d ed Cal CEB 1997).

© The Regents of the University of California

§4.57 b. Purchase Agreement's Title Insurance Provisions

The purchase agreement is ordinarily executed before the buyer has had an opportunity to examine the seller's title. Thus, the agreement should allow the buyer time to examine and approve the exceptions reported by the title company. The seller usually wishes to have the conditions eliminated as soon as possible and will urge a short period of time to review title. The time for approval should run only from receipt of all documents referred to in the preliminary report, not from receipt of the report itself. Sufficient time should be allowed to eliminate objectionable exceptions. See section 3.2 of form 4.171-2 for both a seller's and buyer's form approval provision. Sometimes the agreement instructs the escrow officer to order the preliminary report rather than give the seller this task.

The agreement should set out what is to happen if the buyer disapproves an exception reported by the title company. See section 3.4.2 of form 4.171-4. The effect of the buyer's failure to respond should also be specified. The seller will want the buyer's silence to mean approval, while the buyer will prefer to have it mean disapproval.

PRACTICE TIP: The buyer will want to include in the purchase agreement the right to obtain, 3 to 5 days before the closing, a "date down" of the preliminary report showing any new liens or encumbrances recorded against the property since the date the preliminary report was prepared. See section 3.4.5 of form 4.171-4.

The buyer will usually wish to specify the title company because the buyer will want to obtain coverage from a financially responsible company. Moreover, the buyer may have a long-term working relationship with one particular company. The seller may wish to use the title company that previously insured the title for one of several reasons:

- If title is complicated, to speed preparation of the preliminary report;
- If the seller has a previous relationship with the company, especially when the company is to be the trustee under a deed of trust to the seller; or
- If the seller bought with the title policy a negotiated endorsement, the seller will want the same title company to ensure that the insured exception will again be issued.

The choice of title company may thus be a matter for negotiation, however, the financial condition of the title company should also be considered by the parties in making a selection. The Real Estate Settlement Procedures Act of 1974 (RESPA) (12 USC §§2601-2617), as amended, however, provides that no seller of real property subject to the Act may directly or indirectly require a particular title company as a condition to selling the property. 12 USC §2608. (RESPA is discussed in §15.95.) For a detailed discussion on selecting the title insurer, see California Title Insurance Practice, chap 3 (2d ed Cal CEB 1997). In Northern California, the title company chosen is usually also the escrow holder; in Southern California, the escrow holder is often a different entity from the title insurance company. In most large commercial transactions, however, the title company (or an affiliate) is also the escrow holder. See Title Ins §§3.29-3.30.

Many agreements give the buyer an option to purchase an extended-coverage American Land Title Association (ALTA) policy. The advantage to ALTA coverage is that it discloses matters that can be discerned by an inspection and a survey of the property, such as visible easements (see §4.64), parties in possession, and other off-record matters. See Title Ins §§6.10-6.11. The parties should settle the issue of who is to pay the extra cost of ALTA coverage and any required survey. See §4.134 on allocation of closing costs. See also discussion of ALTA coverage in §15.58 and in Title Ins, chaps 6-8.

© The Regents of the University of California

3. Surveys

§4.58 a. Role of Surveys

It is desirable and often necessary for the buyer to obtain a current survey of the property by a licensed surveyor or civil engineer. A survey will ascertain exact acreage, existence of encroachments and party walls, boundaries (see chap 11), and compliance with setback requirements. Also, lenders usually require surveys as a condition of obtaining an extended-coverage American Land Title Association (ALTA) title insurance policy. If the buyer plans to obtain a loan, counsel should ascertain the lender's survey requirements (including the form of the surveyor's certificate) and obtain the lender's approval of the surveyor to be used.

PRACTICE TIP: It is wise to obtain a survey at the time of purchase, even if neither a loan nor an ALTA title policy is being sought, to avoid the post-closing discovery of an encroachment or other off-record title defect when financing is being sought or the property is put up for sale.

When the sale price is set at a unit rate, rather than a specific amount for the entire parcel, a survey of the property is particularly important. Gross acreage generally includes property such as roads, which revert to the fee owner if abandoned; net acreage excludes such reversionary interests. The seller will generally demand a gross-acreage sale, but the buyer, having no immediate use for the easement, may prefer a net price. This issue is usually resolved by adjusting the price to the parties' satisfaction during negotiations. To avoid future disputes, the parties should make sure that the fee interest under the roads is transferred. If agricultural land is being sold, an accurate survey is needed, especially if the property is being sold at a per-acre price. Counsel should be careful to define whether the price is based on gross or net acreage.

PRACTICE TIP: Buyers often look to their counsel to ascertain the need for a survey (or an expert review of an existing survey, if there is one). The attorney should review with the client the kinds of matters likely to be disclosed by a survey, including encroachments, easement locations, the nature and location of access, and boundary-line discrepancies (including those that may lead to discovery of gaps in the chain of title). Also, counsel should:

- Review the American Land Title Association (ALTA) requirements if an ALTA extended coverage title policy is anticipated;
- Obtain and review with the client cost quotes from the title company for both standard and ALTA extended policies and from the surveyor for both standard and ALTA surveys, so that the client can take these costs into account; and
- Review with the client the desirability of purchasing title endorsements about identification or location of the subject project, *e.g.,* CLTA 116 endorsement (assurances concerning street address and sufficiency of policy plat to show record location and dimensions of land), 116.1 endorsement (assurance that land described in policy is same as shown on plat of survey), and 116.4 endorsement (assurance that land is contiguous to other land).

For discussion of ALTA survey requirements and the types of endorsements available, see California Title Insurance Practice (2d ed Cal CEB 1997).

On the lawyer's role in reviewing surveys, see Title Ins §4.34.

© The Regents of the University of California

§4.59 b. Seller's Knowledge and Notice of Boundaries

Although a survey will clarify any boundary line or encroachment problems in the transaction, the parties are often unwilling to bear its cost. The seller is presumed to know the boundaries of the property being sold, and a misrepresentation of the quantity of land or its geography constitutes fraud. *Wilbur v Wilson* (1960) 179 CA2d 314, 3 CR 770. The seller has a duty to become informed of the boundary lines when selling the property (*Edwards v Sergi* (1934) 137 CA 369, 30 P2d 541) and is not excused from an erroneous representation by evidence that he relied on information from the previous owner (*Wilbur v Wilson, supra*). See also *Williams v Marshall* (1951) 37 C2d 445, 235 P2d 372 (number of acres of citrus trees); *Soderling v Tomlin* (1959) 170 CA2d 169, 338 P2d 946 (location of boundaries); *Piazzini v Jessup* (1957) 153 CA2d 58, 314 P2d 196 (length of lot); *Mills v Hellinger* (1950) 100 CA2d 482, 224 P2d 34 (number of acres). For discussion of a warranty provision on acreage, see §4.99.

A misrepresentation of the location of a boundary line is not fraud if the seller relies in good faith on a misplaced surveyor's mark. *Roland v Hubenka* (1970) 12 CA3d 215, 90 CR 490.

The standard-coverage title insurance policy (see §4.53) does not insure the boundaries, and a survey will be required before the title insurer will provide extended coverage. See California Title Insurance Practice §§4.8, 4.32 (2d ed Cal CEB 1997). On property descriptions generally, see chap 11.

For discussion of a broker's liability for his or her misrepresentations, see §§2.153-2.164.

© The Regents of the University of California

4. Typical Title Issues

a. Taxes

§4.60 (1) Real Property Taxes

The state and federal governments secure the payment of various taxes by placing liens on real property, which make the title unmarketable. In addition, the lien for real property taxes is superior to earlier recorded private liens and to matters for which the real property may become charged or liable, including but not limited to any recognizance, deed, judgment, debt, obligation, or responsibility. Rev & T C §2192.1. See also 3 Miller & Starr, California Real Estate §§11:143-11:175 (3d ed 2000). Tax liens are normally shown on the preliminary report, and buyers who reserved the right to approve title will have an opportunity to approve or disapprove the item.

The most commonly encountered tax lien is for real property taxes for local government general revenue. The tax fiscal year begins on July 1. The tax lien, however, attaches on January 1 of the year preceding the fiscal year for which the taxes are levied. Rev & T C §2192. The tax is payable in two equal installments, which are delinquent if not paid by December 10 and April 10 of the fiscal year for which the taxes are levied. Rev & T C §§2617-2618. If real property taxes are not paid when due, the property securing them is "declared in default" for the unpaid taxes on July 1 (the start of the fiscal year). Rev & T C §§3351, 3436. If the property is not redeemed within 5 years after the date of default (3 years for nonresidential commercial property, unless the county elects to have the 5-year period apply), the tax collector will attempt to sell the property at public auction. Rev & T C §§3691, 3693. See generally 3 Miller & Starr, California Real Estate §§11:143-11:175; Ehrman & Flavin, Taxing California Property (4th ed 2009).

PRACTICE TIP: If the property is subject to a special tax under the Mello-Roos Community Facilities Act (Govt C §§53311-53368.3) or installment assessments to secure bonds issued under the Improvement Bond Act of 1915 (Str & H C §§8500-8887), a seller must use a "good faith effort" to obtain and provide a disclosure notice from the local agency regarding such liens as provided in Govt C §§53340.2 and 53754. CC §1102.6b. See §6.42. In addition, for residential transactions, a disclosure notice regarding the reassessment of the property must be provided under CC §1102.6c. See §6.43.

Real property taxes are usually prorated to the date of closing unless the parties agree otherwise. See section 7.7.5 of form 4.175-7 for a provision on prorating taxes. See §§4.133, 15.43-15.44, 15.57 for discussions of prorations. When a buyer requests a seller to extend the closing date of escrow, the seller may insist that the original closing date be used as the date for prorations. Delinquent taxes should be paid at or before closing to protect the buyer's title.

PRACTICE TIP: If the closing is to occur within a few days after December 10 or April 10, or if current property taxes are delinquent, buyer should request that seller pay the current or delinquent taxes through the escrow holder before or at closing to ensure that the title company has sufficient evidence of payment to allow it to remove the applicable property tax exception from title at closing. Similarly, if a county property tax lien has recorded against the property, buyer should request that a "release of lien" in recordable form from the county assessor's office be delivered to the escrow agent for recording before or at closing.

When the real property being sold is part of a parcel under one assessment, the periods before and after closing present separate problems. For the period before closing, because segregation of taxes is not possible before ownership is transferred, the division must be made by agreement to prorate. For discussion and provisions, see §15.68. For the period after closing, all taxes should be separately assessed to each parcel resulting from the sale. Segregation is authorized by Rev & T C §2821. The application and affidavit of interest must be made during the current fiscal year. A county may prohibit applications during the 10-day period preceding each tax installment delinquent date (December 10 and April 10) and during the 10-day period before June 30 of each year.

© The Regents of the University of California

§4.61 (2) Personal Property Taxes

Personal property is also subject to taxation under California law. Rev & T C §§201, 401. A personal property tax is a lien on real property belonging to the owner of the personal property if it is located on the real property on the lien date. An exception exists if the real property is transferred or conveyed to a bona fide purchaser for value after the lien date but before the assessment on the personal property, and the buyer of the real property did not own, claim, possess, or control the personal property at any time from the lien date until the date on which the assessment was made. Then the taxes on the personal property must be placed on the unsecured roll and will not be a lien on the real property. Rev & T C §2189.

If the personal property or improvement on a parcel is owned by someone other than the fee owner, a statement can be filed with the assessor before the lien date, attesting to the separate ownership, so that the real and personal property will then be assessed on separate bills. Rev & T C §2188.2. When a segregated tax bill is issued, the lien for the tax on the personal property does not attach to the land. The personal property tax lien, however, can attach to other real property owned by the owner of the personal property. Because personal property taxes are usually not shown separately on the preliminary report, the tax bills should be reviewed.

PRACTICE TIP: If the preliminary report shows a lien for personal property taxes, the buyer's lawyer should ascertain who owns the property. If the sale does not include the personal property, the buyer should request a separate assessment under Rev & T C §2188.2. The buyer should either receive the amount of the personal property tax from the seller or some security for payment of the tax if the personal property is owned by someone other than the seller.

If the buyer is purchasing all the personal property, "personal property taxes" should be added to the items to be prorated as is done in section 7.7.5 of form 4.175-7. If the buyer is not purchasing the personal property, the phrase "all personal property taxes shown on the tax bill will be paid by Seller through escrow" should be added to the proration provision. If the buyer is purchasing only some of the personal property, the parties should agree on the value of the property transferred to permit proration of the taxes.

© The Regents of the University of California

§4.62 (3) Federal Tax Liens

In addition to liens for property taxes, which are usually prorated between the buyer and the seller (see §§4.60-4.61), there may also be liens for federal taxes, such as income, withholding, estate, and gift taxes; these liens are not usually paid by the buyer. The seller, however, may be given an opportunity to remove the lien at or before closing without impairing the agreement.

A federal tax lien is not filed against specific property of a taxpayer; it is filed against a named taxpayer and becomes a lien by operation of law. On assessment, federal taxes become a lien against all of the taxpayer's property or rights to property. IRC §6321. Federal tax lien procedures that do not provide for preattachment hearings have been upheld in the face of challenges contending that they deny property owners due process. *Baldassari v U.S.* (1978) 79 CA3d 267, 144 CR 741. The lien is not valid against a buyer of real property unless notice of the lien is filed with the recorder of the county where the property is located. IRC §6323.

A special lien for estate and gift taxes exists without assessment and includes taxes not paid when due. IRC §6324. There are also special lien provisions for deferred estate taxes (IRC §6166) and for additional estate taxes attributable to a farm or a closely held business valuation (IRC §§6324A-6324B). If unassessed estate tax appears as a possible lien on the preliminary report, written application for its release should be made to the IRS district director under Treas Reg §301.6325-1(c). If a notice of tax lien was filed and the tax was or will be paid from escrow, arrangements can be made to release the lien.

When the taxpayer's name is the same as another property owner in the county, some confusion may occur. On a showing of the facts, a certificate of nonattachment of federal tax lien may be obtained (from the chief of special procedures staff in the district director's office), certifying that the filed lien does not attach to a particular parcel of property. A taxpayer (against whom a federal tax lien has been filed) who is refinancing or purchasing property through third party financing may obtain a similar certificate. This certificate permits the taxpayer to complete the transaction by certifying that the lien does not attach to the lender's interest in the property.

PRACTICE TIP: Instructions on how to apply for a Certificate of Discharge of Property From Federal Tax Lien may be found on the Internal Revenue Service website. The payoff amount on a lien can be ascertained by telephoning the IRS. The website and telephone number are in the Directory. The owner or intended buyer may obtain this information even if he or she is not the taxpayer against whom the lien is filed. Treas Reg §301.6323(i)-1(c). If federal tax lien problems are suspected, the purchase and sale agreement should provide sufficient time before closing to resolve them.

© The Regents of the University of California

§4.63 b. Special Assessments

The lien of a special assessment to pay for the construction or maintenance of some public improvement, such as a lighting district, a road, or a sewer, arises when a notice of assessment or special tax lien is recorded. Str & H C §§3114-3115. An assessment lien generally affects only the parcels benefited by the improvement. Assessment liens have priority over private liens and matters for which the real property may become charged or liable, including, but not limited to, any recognizance, deed, judgment, debt, obligation, or responsibility. Rev & T C §2192.1; see California Title Insurance Practice §8.15 (2d ed Cal CEB 1997). If assessments are not paid when due, the property may eventually be sold by the tax collector. Rev & T C §3691.

Problems can arise when an improvement has been completed but the government has yet to levy an assessment. In that event, the lien would not be listed as an exception on the preliminary report, because it would not be a lien of record. The buyer would be liable for such an assessment and would have no recourse against the title insurance policy. This matter is often covered by a seller's warranty that will survive close of escrow. For a warranty, see form 4.173-1, Alternative 1, section 5.1.14 (buyer's form of seller's warranties); for a standard survival of closing provision, see form 4.173-3; for a seller's form providing for limited survival of representations and warranties after closing, see form 4.173-4.

PRACTICE TIP: The treatment of assessments is negotiable. The seller usually wants the buyer to bear the burden of the assessment because the buyer will benefit from the improvement. The buyer will argue that the improvements increased the value of the property and were taken into consideration in arriving at the purchase price and should therefore be paid by the seller at closing.

© The Regents of the University of California

§4.64 c. Easements

An encumbering easement usually destroys marketability of title. *Zlozower v Lindenbaum* (1929) 100 CA 766, 281 P 102. A visible easement, however, is not treated as a breach of the covenant to sell free of encumbrances (CC §1113), because the parties are presumed to have contracted with it in mind. *Rustigian v Phelps* (1923) 190 C 608, 213 P 957; *McCarty v Wilson* (1920) 184 C 194, 193 P 578. Counsel for the buyer must ascertain what easements exist, obtain and review the pertinent documents, and explain their significance to the buyer. The buyer must then decide whether the property is suitable for the intended use.

Ascertaining easements requires more than merely reviewing the preliminary report and the underlying documents. Standard-coverage (CLTA) title insurance protects the insured from losses resulting from easements only if they are revealed in the public record. It excludes interests that are not shown in the public record but that are ascertainable by inspecting the property or inquiring of persons in possession. For discussion of evaluating easements in the title insurance context, see California Title Insurance Practice §5.10 (2d ed Cal CEB 1997). An ALTA policy provides further protection by insuring against defects that are discoverable from an inspection of the property. Both the CLTA and ALTA policies exclude defects known to the insured party but unknown to the title company. On ALTA title insurance policies, see Title Ins, chap 6.

If the buyer does not wish to incur the expense of ALTA coverage, the premises must be inspected and persons in possession questioned about the rights of others to use the property. Protection may also be obtained by including in the purchase and sale agreement the seller's warranty against easements not of record.

An easement that is sufficiently visible to create a prescriptive or an implied easement will bind subsequent buyers, even if it is not shown on the record. *Ocean Shore R.R. v Spring Valley Water Co.* (1933) 218 C 86, 21 P2d 588; *Lindsay v King* (1956) 138 CA2d 333, 292 P2d 23. The following are examples of visible easements:

- Portions of a railroad grade and trestle (*Ocean Shore R.R. v Spring Valley Water Co., supra*);
- A paved portion of property used for access to an adjacent gas station (*Amerco, Inc. v Tullar* (1960) 182 CA2d 336, 6 CR 71);
- Standpipes for a water pipeline (*Johnson v Cella* (1953) 122 CA2d 72, 264 P2d 98); and
- A utility easement with wires running 80 feet above the property and visible from various parts of the property (*Alcan Aluminum Corp. v Carlsberg Fin. Corp.* (9th Cir 1982) 689 F2d 815).

Such visible evidence puts the buyer on inquiry notice, and the buyer can neither assume that the use is abandoned nor be satisfied with the owner's opinion that the easement will not be used. The buyer is charged with constructive knowledge of facts that would be disclosed if a reasonable inquiry were made. *Ocean Shore R.R. v Spring Valley Water Co., supra*.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.65 d. Party Walls

§4.65 d. Party Walls

If a structure on the property has a wall in common with a structure on adjoining property, the buyer has at least three concerns:

- The wall may affect title (possibly rendering it unmarketable). The right to use a party wall is an easement. CC §801(12). It may not render title unmarketable if the party wall stands equally or partly on the adjoining land and mutual rights and obligations exist, but it may render title unmarketable if the wall stands entirely on the subject property. 3 Casner, American Law of Property §11.49 (1952); Anno, *Marketable Title—Party Walls*, 81 ALR2d 1020 (1962).
- The wall may limit the buyer's use. The right to demolish an existing structure is subject to the buyer's obligation to maintain the party wall. *Nippert v Warneke* (1900) 128 C 501, 61 P 96.
- The wall may subject the buyer to expenses and obligations in connection with the wall. Without an agreement to the contrary, each owner is entitled to increase the height and width of the wall as long as no damage is done to the other structure or to the wall itself. *Tate v Fratt* (1896) 112 C 613, 44 P 1061. Either owner may use its part of the wall for advertising, may deepen the foundation, and may rebuild a dilapidated wall. Injury to the wall is actionable (*McCarthy v Mutual Relief Ass'n* (1889) 81 C 584, 22 P 933), as is removal (*Nippert v Warneke, supra*).

A wall may stand entirely on one parcel and still be a party wall. See *Tate v Fratt, supra*. If it is a party wall, the use of each parcel must not impair the cross-easements of support and beam rights (CC §801(12)) of the adjoining owner. A party wall may give the buyer an easement on the adjoining property. A buyer who considers the party wall an asset should be aware that destruction by fire or other casualty terminates the easements and related rights and duties unless they are preserved by agreement. 5 Powell, The Law of Real Property §691 (1986).

In view of the risks involving party walls, any wall that appears to support a structure on adjoining land as well as one on the subject property is a signal to the buyer to ascertain the following:

- Whether the wall supports both structures;
- The exact location of the boundary line in relation to the wall (normally fixed by a survey); and
- The existence and provisions of any express or implied agreement between the seller or the seller's predecessor and the adjoining property owner or its predecessor.

On implied agreements, see *Nippert v Warneke, supra; Bank of Escondido v Thomas* (1895) 5 CU 94, 41 P 462; *Guttenberger v Woods* (1876) 51 C 523.

If no express agreement exists, it may be possible to negotiate and execute one before the close of escrow. On provisions for party wall agreements, see Belsheim, Modern Legal Forms §§6482-6510 (1979).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.66 e. Covenants, Conditions, and Restrictions

§4.66 e. Covenants, Conditions, and Restrictions

Declarations of covenants, conditions, and restrictions (CC&Rs) are frequently recorded in connection with the development of residential subdivisions or office or industrial parks. CC&Rs are intended to restrict uses in the entire development for the mutual benefit of all landowners.

- "Covenants" are promises that, if not performed, give rise to an action for breach. For remedies on breach, see California Real Property Remedies and Damages, chap 4 (2d ed Cal CEB 2002).
- "Conditions" are limitations on the full and unqualified enjoyment of the right or estate granted. *Zlozower v Lindenbaum* (1929) 100 CA 766, 281 P 102. If the conditions are enforceable, their violation terminates the estate or gives a right of termination.
- The term "restrictions" does not include easements (see *Zlozower v Lindenbaum, supra*), except in the sense that restrictions are considered to be either "negative" easements or equitable servitudes (*Sackett v Los Angeles City Sch. Dist.* (1931) 118 CA 254, 5 P2d 23). Not all purported restrictions are enforceable. Some restrictions are unenforceable on constitutional or public policy grounds. See, *e.g., Shelley v Kraemer* (1948) 334 US 1, 92 L Ed 1161, 68 S Ct 836; *Cumings v Hokr* (1948) 31 C2d 844, 193 P2d 742 (refusal to enforce racial restrictions).

A buyer at a trustee's sale foreclosing a lien senior to the declaration of restrictions is not bound by the CC&Rs, because the sale extinguishes the junior restrictions. *Sain v Silvestre* (1978) 78 CA3d 461, 144 CR 478, disapproved on other grounds in *Reynolds Metals Co. v Alperson* (1979) 25 C3d 124, 129, 158 CR 1.

If there is a common plan for ownership of property in a subdivision, and that plan includes CC&Rs that were recorded before the sale of the property, they are enforceable even if they are not cited in a deed or other document at the time of sale. In *Citizens for Covenant Compliance v Anderson* (1995) 12 C4th 345, 47 CR2d 898, the court held that because the CC&Rs (1) were recorded before any of the parcels were sold (thus providing constructive notice to subsequent buyers), (2) stated an intent to establish a general plan for the subdivision that would be binding on all buyers and their successors, and (3) described the property the CC&Rs were to govern, the fact that the individual deeds did not refer to the CC&Rs was not fatal to their enforceability.

If there is no agreement to the contrary, the existence of CC&Rs in the chain of title generally renders title unmarketable and entitles the buyer to withdraw from the transaction. *Tandy v Waesch* (1908) 154 C 108, 97 P 69. Restrictions imposed by law, however, do not impair title, because the parties are considered to have contracted under applicable law. See *Hartman v Rizzuto* (1954) 123 CA2d 186, 266 P2d 539 (holding, nevertheless, that facts of case relieved buyer of consequences of rule on restrictions imposed by law). Not all restrictions impair the value of the property—some even enhance value by preventing objectionable use of neighboring parcels.

PRACTICE TIP: To ensure that the CC&Rs are acceptable to the buyer in light of the intended use of the property, the agreement should give the buyer the right, as part of its title review, to decide within a reasonable time whether the restrictions are enforceable and tolerable.

© The Regents of the University of California

§4.67 f. Encroachments

An encroachment by improvements (such as buildings, parking lots, or retaining walls) will render title unmarketable whether it is by or on the property in question. See 13 Witkin, Summary of California Law, *Equity* §56 (10th ed 2005). An accurate survey will disclose the existence of any encroachments. An encroachment on the subject property not only limits the buyer's use but may ripen into a prescriptive easement. *Jones v Harmon* (1959) 175 CA2d 869, 1 CR 192. Moreover, an encroachment on the subject property exposes the buyer to possible liability for its removal or damages. *Brown Derby Hollywood Corp. v Hatton* (1964) 61 C2d 855, 40 CR 848. A survey will also disclose whether improvements encroach on easements on the property. The encroachment may violate the terms of the easement or it may be subject to removal by the easement holder.

On title insurance endorsements for encroachments, see California Title Insurance Practice, chaps 7-8 (2d ed Cal CEB 1997).

© The Regents of the University of California

§4.68 g. Adverse Possession

Title by adverse possession may arise in the following forms:

- An attempt by the seller to base title on adverse possession; or
- An asserted interest by a third party adverse to the interest the buyer expects to acquire from the seller.

In California, a title by adverse possession is apparently considered unmarketable and need not be accepted by a buyer. See *Gwin v Calegaris* (1903) 139 C 384, 73 P 851; *Benson v Shotwell* (1890) 87 C 49, 25 P 249. The practice of requiring "marketable record title" in the agreement, although it would oblige the seller to reduce the adverse interest to record title, may have the undesired effect of waiving record defects unless title insurance is required. Section 6.1.1 of form 4.174-1 requires the seller to deliver "marketable fee simple title" and procure title insurance. This requirement in effect obligates the seller to reduce title to judgment and record it, and it protects the buyer from other record defects.

Ordinarily, adverse interests do not appear on the preliminary report unless they appeared in a recorded judgment or lis pendens in a quiet title action by or against the adverse interests. The buyer is considered to have taken subject to these interests if an examination of the premises would have revealed them (see §§4.64, 4.71). Therefore the buyer should make a physical inspection of the property and consider obtaining a survey.

An ALTA extended-coverage title policy (and the required survey) will insure against adverse claims by parties in possession. On title insurance protection against adverse interests, see California Title Insurance Practice §3.29, chap 7 (2d ed Cal CEB 1997).

© The Regents of the University of California

§4.69 h. Mechanics' Liens

Persons who supply labor or materials to improve real property are entitled to a mechanics' lien against the property to secure payment. CC §§3109-3154. See generally California Mechanics' Liens and Related Construction Remedies (3d ed Cal CEB 1998). Such a lien makes title unmarketable. The lien takes its priority as of the date work commences on the project. The contractor must record a lien claim within 90 days after completion of the work if no notice of cessation or completion is filed, or 30 days after recordation of a Notice of Completion or Cessation (60 days if original contractor). CC §§3115-3116. An action to foreclose the lien must be brought within 90 days after the lien is recorded unless the time is extended by a recorded grant of credit. CC §3144. The procedure for cancellation of a mechanics' lien is set forth in CC §3154.

If the preliminary report shows any mechanics' liens or an action to foreclose a mechanics' lien, the seller should be required to clear the lien from the preliminary report. Standard form title insurance covers only matters disclosed by the public record. A buyer should therefore obtain a warranty from the seller that no work has been or will be performed during the 90-day period before the close of escrow and that the seller knows of no mechanics' liens other than those shown on the record. If improvements were completed within 90 days before close of escrow, unrecorded mechanics' liens may exist. If so, a notice of completion should be recorded immediately and close of escrow delayed until the 30-day period for filing lien claims has expired. The CLTA 101.1 endorsement insures the buyer against any liens arising from work referred to in the notice of completion. On the CLTA 101.1 endorsement, see California Title Insurance Practice §§7.88-7.89 (2d ed Cal CEB 1997).

If it is not possible to delay the closing for 30 days or if construction continues to the closing date, other devices are needed to protect the buyer from lien claims. Assuming that the contractor did not post a completion bond for the job before its commencement, the buyer can obtain some protection by requiring the remainder of the construction funds to be deposited in escrow and instructing the escrow holder to pay only on receipt of paid bills and partial or complete lien waivers. See §15.93. Another choice is to leave a fund in escrow for a period after closing to be used to clear any liens that may appear. The lender and the buyer, respectively, are protected for work under construction or completed as of the title policy date by CLTA 101.3 and 101.4 endorsements. The title company may, however, require an indemnity agreement or a bond to ensure payment of claims that may arise. Other endorsements are available that give more limited coverage or apply to unusual situations. On CLTA endorsements 101.3 and 101.4 and other mechanics' lien endorsements, see Title Ins §§7.88-7.89, 8.83-8.84.

See section 4.4 of form 4.172-4 for a seller's covenant to keep the property free of mechanics' liens.

© The Regents of the University of California

§4.70 i. Matters Discoverable by Inspection

The buyer is charged with constructive notice of matters discoverable by inspection of the property. The usual California Land Title Association policy does not insure the physical location of the parcel or against unrecorded easements or other claims of right that an inspection would reveal. See California Title Insurance Practice §3.8 (2d ed Cal CEB 1997).

PRACTICE TIP: To guard against these hazards, the purchaser should make, or have experts make, a physical inspection of the property. If uncertainties exist about boundaries, encroaching improvements, or similar problems, inspection may not be enough; a survey may be needed. On surveys, see §§4.58-4.59.

© The Regents of the University of California

E. Leases

§4.71 1. In General

An outstanding lease of any part of the property renders title unmarketable. *Dennis v Overholtzer* (1960) 178 CA2d 766, 3 CR 193, disapproved on other grounds in *Ellis v Mihelis* (1963) 60 C2d 206, 221, 32 CR 415. Most agreements, however, provide for assumption of existing leases. Because unrecorded leases do not appear on a preliminary report, inquiries must be made of persons in possession to ascertain the tenants' identities and their rights with respect to the owner. The buyer's counsel must study the leases carefully to ascertain the parties' respective rights. Oil and gas leases are not considered leases but rather a profit à prendre, giving an interest in land. *Wolf v Price* (1966) 244 CA2d 165, 52 CR 889. For a checklist of due diligence materials the seller must deliver to the buyer in sales of properties with commercial leases, see App C.

For further discussion of leases affecting title to property, see California Title Insurance Practice §§5.14, 6.23 (2d ed Cal CEB 1997).

© The Regents of the University of California

§4.72 2. Purchase Free of Leases

If the seller is to deliver the property free of tenants, and a tenant's lease is expiring, the lease must be reviewed to learn the following:

- When the term ends;
- Whether the tenant has an option to extend, a right of first refusal, or an option to purchase the property; and
- What the tenant can remove from the premises on departure.

If the seller has, or plans to enter into, a lease termination agreement with the tenant, that agreement should also be reviewed.

Timing problems arise if the property is to be acquired free of tenants. On termination and eviction procedures generally, see California Landlord-Tenant Practice, chaps 7-13 (2d ed Cal CEB 1997); Office Leasing: Drafting and Negotiating the Lease §29.7 (Cal CEB 1996); Geyer, *Ten Steps to Success in Commercial Evictions*, 20 CEB Real Prop L Rep 97 (Apr. 1997). If the tenants are on a month-to-month basis, a 30-day notice is required. CC §1946. If the lease has expired, no notice is needed. CCP §1161(1). If the tenants do not leave, unlawful detainer proceedings (CCP §1161) must be instituted, which may be time consuming. The seller does not want to force out tenants without assurance that the buyer will perform, while the buyer wants possession as soon after closing as possible. The following are possible solutions:

- Placing a sufficient deposit in escrow and removing all other conditions to closing so that the seller feels secure that the buyer will perform, but if the buyer does not, there will be funds to pay damages;
- Closing escrow with the tenants in possession and retaining some of the seller's proceeds to pay the buyer's liquidated damages if the tenants do not vacate on time; or
- Closing escrow immediately, with the buyer having to remove the tenants in return for a reduction in the purchase price.

If tenants are to remain after the closing, the rents should be prorated and security deposits transferred to the buyer.

PRACTICE TIP: The possibility that local rent control or condominium conversion ordinances may limit eviction of residential tenants should not be overlooked. See §6.60. For discussion of such ordinances, see Landlord-Tenant, chap 7.

© The Regents of the University of California

§4.73 3. Purchase Subject to Leases

Unless a lease provides to the contrary, the landlord may sell the property to another with the leases in place. The buyer succeeds to the seller's position in relation to the tenant without the necessity for the tenant's attornment. See CC §1111; *Diepenbrock v Luiz* (1911) 159 C 716, 115 P 743. Assignments of leases, however, merit more than a perfunctory preparation by escrow holders. The seller may have either a cause of action for waste that should be assigned to the buyer along with the lease (see *Hill v Pinque* (1922) 56 CA 245, 204 P 1097) or rights on the land that will not pass without express assignment (see *Chipman v Emeric* (1855) 5 C 49). Moreover, because the buyer is bound by the seller's interpretation of the leases and by any waivers the seller has made (*Doll v Maravilas* (1947) 82 CA2d 943, 187 P2d 885), the buyer may need the protection of the seller's warranties or the tenants' estoppel certificates. For these reasons, the buyer should reserve the right either to prepare the assignments or to approve them. For a form assignment of leases, see App I.

If current tenants will remain in possession, the buyer should review all leases and any related documents, such as amendments and correspondence. Counsel should examine and outline the following provisions of each lease:

- Term;
- Rent;
- Renewal rights;
- Inflation adjustment provisions;
- Landlord's right to pass increased taxes and operation costs on to the tenant;
- Any options (*e.g.*, to extend the lease term, to lease additional space, to purchase); and
- Any uncompleted obligations of the landlord to make improvements to the premises under any lease.

An estoppel certificate (see App K for form) should be obtained from each tenant to confirm (1) the basic terms of the lease (including term and rent), (2) the absence of defaults by either landlord or tenant, and (3) the absence of other agreements between landlord and tenant. See form 4.174-1, section 6.1.4, Alternatives 1-2, for provisions requiring the seller to deliver estoppel certificates to the buyer. The certificate estops the tenant from claiming otherwise after the closing. See Evid C §622. The leases should also be checked to determine whether the content of the estoppel certificate has been prescribed in the lease. It is not uncommon for large credit tenants to negotiate the content of the certificate as part of their lease negotiations. In *Plaza Freeway Ltd. Partnership v First Mountain Bank* (2000) 81 CA4th 616, 96 CR2d 865, a tenant was estopped from contradicting a lease termination date in an estoppel certificate given to the landlord when the landlord bought the building subject to the lease; as a result, the tenant lost its opportunity to exercise an option to extend the term of the lease (under the original lease) because it failed to do so before the termination date in the estoppel certificate.

The buyer should also obtain a letter from the seller to be delivered after the closing, instructing the tenants to pay rent to the buyer. For a form of a letter to tenants, see App L. On considerations applicable in commercial leasing situations, see generally Retail Leasing: Drafting and Negotiating the Lease (Cal CEB 2007); Office Leasing: Drafting and Negotiating the Lease (Cal CEB 1996).

PRACTICE TIP: Buyers and their lenders usually want estoppel certificates dated near the closing to ensure that tenants are not in default at the closing. Sellers prefer to deliver estoppel certificates earlier to eliminate possible grounds for disapproving or modifying the purchase and sale agreement if the estoppel certificates reveal unexpected problems.

Often in multi-tenant properties, the parties agree to accept estoppel certificates from less than 100 percent of the tenants if the seller warrants the information that would have been in the tenant's certificate for the tenants who did not sign an estoppel certificate, but buyers should always require originally executed estoppels for major credit or anchor tenants. This provision should dovetail with the requirements of the buyer's lender, if they are known at the time the provision is drafted. See form 4.174-1, section 6.1.4, Alternatives 1-2.

If there are more than a few simple leases, it is common for the buyer to require the seller to prepare and warrant, as accurate and complete, a rent roll or summary that includes, for each lease, an identification of the rent and other charges such as triple net expenses, the terms and option to extend, and other key information. See form 4.171-1, Alternative 2, section 3.1.7, and form 4.174-1, section 6.1.4, Alternatives 1-2, for provisions requiring the seller to deliver a rent roll. Thus, the buyer can rely on the rent roll before receiving estoppel certificates near the end of the escrow period. Other assurances that could be covered by the rent roll or the warranty in this form are the following:

- No tenant has paid advance rent;
- No tenant has any right of first refusal or any option to lease or purchase the property;
- None of the rents due or to become due under any of the leases will be assigned, encumbered, or subject to any lien at the closing;
- No leasing or brokerage fees or commissions will become due or owing after the closing on any lease in effect on the closing date; and
- Any improvements to be made by the seller that are contemplated under or required by the leases have been completed.

© The Regents of the University of California

§4.74 4. Agricultural Leases

If the transaction pertains to agricultural land, the buyer should be advised that a tenant holding under an expired lease cannot always be ousted quickly. A tenant of agricultural land who holds over for more than 60 days after expiration of the term, without receiving a demand for possession or notice to quit, can continue in possession for another year on the same terms as the prior year. CCP §1161(2).

© The Regents of the University of California

§4.75 5. Ground Leases

If the buyer is purchasing the tenant's interest in a ground lease, counsel should verify the following:

- The seller can transfer the tenant's interest in the lease;
- There are no defaults under the lease or, if there are, that they have been waived;
- There are no lease provisions that could cause early termination of the lease; and
- There are no provisions calling for removal of improvements from the property at the end of the term.

The nature of any restrictions on the use or subleasing of the property should also be reviewed. Counsel should also ascertain whether the ground lease contains the necessary provisions to enable the tenant to obtain financing on the leasehold. See Nellis, *Drafting or Reviewing a Ground Lease to Make It "Mortgageable,"* 1 CEB Real Prop L Rep 49 (May 1978). The seller must also deliver an assignment approved by the ground lessor (if required by the lease) before the closing. For considerations relating specifically to ground leases, see Ground Lease Practice (2d ed Cal CEB 2009).

© The Regents of the University of California

§4.76 6. Third Party Contracts

The buyer should review all third party contracts relating to the property and its operations, including all service and maintenance agreements (*e.g.*, elevator, janitorial, landscaping, fire protections, parking lot maintenance, security) and asset or property management agreements, to determine whether to continue with such service providers after closing or to seek termination of any of the contracts. The contracts should be reviewed for their term and assignability and, if warranted due to the nature or cost of such service, buyer should meet with or speak to representatives of these service companies. Seller may resist terminating longer term contracts if an early termination fee or buyout will be involved. Contract approval or disapproval generally occurs during the due diligence period and proof of termination of the disapproved contracts becomes a closing condition. See form 4.173-1.

© The Regents of the University of California

F. Physical Condition of Property

§4.77 1. In General

Of equal importance with the state of title is the physical condition of the property and its suitability for the buyer's intended use. Ascertaining the property's condition may require time-consuming work, such as soil tests, engineering studies, hazardous waste reviews, surveys, and termite inspection. It is important that the buyer have the right to approve the results of this work. If the inspections will take a long time, the buyer may wish to obtain an option to buy and conduct tests during the option period. On options, see chap 8. Buyers usually want to avoid purchasing property on an "as is" basis, while sellers usually prefer to sell on that basis. For an "as is" provision for a seller-oriented form, see form 4.173-5. How this conflict is resolved depends on the parties' needs and negotiating strengths.

A first step in ascertaining physical condition is to obtain all plans, specifications, and reports that have already been done and are in the seller's possession. These plans may reveal conditions that will lead the buyer to decide against purchasing; if they do not, the buyer should have an architect or engineer review the reports and decide whether additional or updated information is needed.

EXAMPLE: Although soil does not usually change, previously conducted soil tests may not be conclusive for the particular buyer, because they may have been performed for a different use, for a different location on the property, or under outdated building codes.

The nature of the property and its intended use will dictate the studies needed. For commercial property, the buyer should retain a structural engineer and such other professionals as the engineer suggests to check not only the structure of the building but also the roof; the electrical, plumbing, heating, air-conditioning, and ventilation systems; the elevators; the condition of exterior and interior glass; and all other components of the building. The engineer should survey the building to learn how it conforms to present or proposed housing and building codes, and outline the work and expense necessary to bring the building up to code. If undeveloped land is being purchased, soil tests need to be made to determine the quality, condition, and suitability of the soil for the intended use. On agricultural land, tests on wells may be needed in addition to inspections of improvements on the property.

NOTE: The presence of fill must be disclosed when raw land is being sold. *Massei v Lettunich* (1967) 248 CA2d 68, 56 CR 232; *Clauser v Taylor* (1941) 44 CA2d 453, 112 P2d 661. If the property is already improved, failure to disclose that the buildings stand on filled ground is actionable. *Central Mut. Ins. Co. v Schmidt* (1957) 152 CA2d 671, 313 P2d 132.

Engineering studies for land development that will affect the flow of surface waters are especially important in view of the holding in *Keys v Romley* (1966) 64 C2d 396, 50 CR 273, that an upper landowner who changes a natural drainage system may be liable to a lower landowner even if the upper landowner's actions are reasonable. The issue of reasonable or unreasonable use is a question of fact after considering the relevant circumstances, including the amount of harm caused, the ability of the person making the change to foresee the harm, and the purpose for which he or she acted. If both owners acted reasonably, the burden of the damage is generally imposed on the upstream owner. For a discussion of the application of California's modified civil-law rule of reasonable use, see 3 Miller & Starr, California Real Estate §§14:20-14:21 (3d ed 2000). For application of the "reasonable" rule to public entities in inverse condemnation cases, see *Locklin v City of Lafayette* (1994) 7 C4th 327, 27 CR2d 613; but see *Arreola v County of Monterey* (2002) 99 CA4th 722, 122 CR2d 38 (in an inverse condemnation action by downstream property owners who were flooded because of state's inadequate maintenance of levee system, public policy required application of strict liability standard rather than reasonable standard).

© The Regents of the University of California

§4.78 2. Buyer's Inspection Rights

Most agreements give the buyer the right to inspect and test the property; see section 3.5.2 of form 4.171-5. The seller may wish to approve the dates and times of inspections and tests to minimize interference with the seller's use of the property. The requirement that a notice of disapproval must describe the alleged defect with particularity is intended to give the seller an opportunity to cure the defect, if possible. If tenants are on the property, the seller's right to authorize the buyer's entry may be subject to the tenants' rights. In this event, the purchase agreement should set appropriate limitations.

Often, the buyer will agree to deliver copies of any studies in its possession to the seller if the transaction does not close. The information is of no further use to the buyer, but it may be useful to the seller and to future buyers.

The seller should be protected from any liability for costs of the tests as well as damages that may arise, such as injury to persons or property arising from entry onto the seller's property. It is customary for the buyer to include a provision indemnifying the seller for damages or injury. See section 3.5.2 of form 4.171-5.

NOTE: The buyer may want to amend the indemnity to provide that the buyer will not be liable for (1) the buyer's (or its agents') exacerbation of existing conditions if the buyer (and its agents) exercised reasonable care to detect such conditions and avoid further damage or harm, or (2) the results of disclosing any existing conditions or contamination discovered during the buyer's inspections.

The seller may wish to have the buyer's obligations secured by a performance bond to ensure that any mechanics' liens arising from the buyer's work will not become the seller's problem. The seller may also require persons working on the property to carry liability insurance.

PRACTICE TIP: The seller should post and record notices of nonresponsibility within 10 days after work is commenced, as provided by CC §3094. The seller should insist that the buyer's deposit in escrow be large enough to cover any mechanics' liens. If the sale does not close, the seller should require delivery of valid lien waivers from the contractors who worked on the property before the buyer's deposit is returned. The seller can learn which contractors have lien rights from the preliminary notices contractors are required to give under CC §3097.

On mechanics' liens generally, see California Mechanics' Liens and Related Construction Remedies (3d ed Cal CEB 1998). On liability insurance, see generally California Liability Insurance Practice: Claims & Litigation (Cal CEB 1991).

© The Regents of the University of California

§4.79 3. Structural Pest Control Inspection

Damage caused by termites, dry rot, or fungus can be expensive to repair, and there is no implied warranty that the property will be free of latent defects unknown to the seller. *Murphy v Sheftel* (1932) 121 CA 533, 9 P2d 568. The buyer should require a property inspection by a company registered with the Structural Pest Control Board before close of escrow. On how to contact the board, see the Directory.

Under CC §1099, the seller must furnish the buyer with a copy of any structural pest control inspection report obtained by the seller if such a report or certificate is either a condition of the contract or a requirement for financing. See also 10 Cal Code Regs §2905.

The issues of which party will choose the pest control inspector, pay for the report, and pay for any remedial or preventive work are all subject to negotiation. A common practice is for the buyer to pay for the inspection and report and for the seller to pay for corrective work. Preventive work benefits the new owner, however, and is usually paid for by the buyer (or credited against the purchase price) if the buyer elects to have it done before closing. Other forms permit the buyer to inspect the property and either accept or reject it without a provision for payment for corrective work.

If the buyer bears the cost of corrective work, or if the seller is to pay and fears that the cost of such work will be great, a provision can be inserted allowing the party paying for the repairs to terminate the transaction if the estimated cost exceeds a certain sum. The seller should always either obtain a report and a price quotation for any corrective work before executing a purchase and sale agreement or should insert a provision limiting the amount of its liability for such work. Even if the seller is willing to pay for the repairs, the buyer may wish to retain the right to terminate if the report indicates that extensive corrective work is required, because corrective work may not eliminate the problem.

If the work is to be completed before the close of escrow, it may be necessary to include a provision extending the closing date if repairs are extensive. An alternative is to provide that, if repairs are not completed by the closing date, an amount equal to the cost of the repairs will be held in escrow to be released when the escrow holder receives a notice of work completed under Bus & P C §8519(b) and the buyer indicates that the work was performed satisfactorily.

If the seller is to pay for any work, a lien waiver from the contractor should be obtained so that title insurance can be issued without a mechanics' lien exception.

© The Regents of the University of California

§4.80 4. Hazardous Substances

The Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA or "Superfund") (42 USC §§9601-9675), as amended, imposes liability on owners or operators of properties for the cost of remedial action when there is an actual or threatened release of hazardous substances into the environment. The term "hazardous substance" is defined in CERCLA and includes a long list of substances, some of which may be found in common household products.

The buyer's counsel should explain that, by merely purchasing a property, the buyer may become liable for its clean-up costs, even if someone else actually disposed of a hazardous substance on the property. The buyer may be protected from this risk by making "appropriate inquiry" into the condition of the property before acquiring it. If, after appropriate inquiry, the buyer neither discovers nor has any reason to be aware of a hazardous substance on the property, the buyer will be deemed an "innocent" landowner. The risk exists, however, that if a hazardous substance existing on the property was not found, a court would rule that the inquiry was not "appropriate." The buyer's best protection, therefore, is to obtain an environmental report on the property, to investigate the property's historical use, and to provide as a condition of closing that no hazardous substance exists on the property. The buyer will also want to obtain a warranty from the seller that no hazardous substances are on the property. See form 4.173-1, Alternative 1, section 5.1.16. The seller, however, will want to be relieved of future liability on the property once it is sold. See chap 7 for discussion of hazardous substance considerations and illustrative contract provisions.

In addition to federal requirements, Health & S C §25359.7 requires sellers of nonresidential real property to disclose in writing to buyers any hazardous substance that they know or have reason to believe is located on or beneath the surface of the property. Failure to so notify a buyer will subject the seller to actual damages and a fine of up to $5000 for each willful failure to notify the buyer of a release of a material amount of a hazardous substance.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.81 5. Natural Hazard Disclosure Statement

§4.81 5. Natural Hazard Disclosure Statement

The transferor of real property is required to disclose to the transferee whether the property lies within any of the following hazard zones:

- Flood (Govt C §§8589.3-8589.4);
- Fire (Govt C §51183.5);
- Wildlands fire (Pub Res C §4136);
- Earthquake fault (Pub Res C §2621.9); or
- Seismic (Pub Res C §2694).

Generally, disclosure must be made if (1) the transferor, or the transferor's agent, has actual knowledge that the property is within a hazard zone, or (2) the property is shown on a map or list of hazard zones posted at the offices of the county recorder, county assessor, and county planning agency.

In transactions involving either real property improved with one to four dwelling units or the resale of a manufactured home or mobilehome, CC §1103.2 requires that any necessary disclosure be made either (1) by using the form of the Natural Hazard Disclosure (NHD) statement set forth in CC §1103.2(a) or (2) under CC §1103.2(e), by way of a Local Option Real Estate Disclosure Statement delivered in the form set forth in CC §1102.6a. See §6.38. For a copy of the statutory form, see §6.39. If the seller fails to deliver the statement before closing, the buyer may terminate the transaction. 84 Ops Cal Atty Gen 141. After closing, the buyer's remedy is limited to actual damages. CC §1103.13.

In transactions involving purely commercial property or residential property with more than four dwelling units, CC §1103's requirement of use of the statutory form does not apply; nonetheless, natural hazards known to the seller or seller's agent or shown on a list or map maintained by the county must be disclosed. The form in App N was adapted from the NHD form in CC §1103.2(a). Unlike the statutory form, the language in App N contemplates that it will be part of a purchase and sale agreement and characterizes the statements as "disclosures," not "representations." This wording may make it more palatable to commercial sellers, who generally wish to reduce the number of representations they make.

The information required in the NHD Statement is now commercially available. See §6.49.

PRACTICE TIP: Other disclosure requirements may also apply to natural disaster hazards. For example, Govt C §8893.2 requires that the seller or its agent give a copy of the Commercial Property Owner's Guide to Earthquake Safety (described in Bus & P C §10147) to all buyers of any precast concrete or reinforced masonry buildings with wood frame floors or roofs built before January 1, 1975.

See Directory for sources of maps or other information on natural hazards.

© The Regents of the University of California

§4.82 6. Toxic Mold Disclosure Requirements

The Toxic Mold Protection Act of 2001 (Health & S C §§26100-26156) enacted disclosure and remediation requirements regarding mold in buildings. It requires the Department of Health Services to study the adverse health effects of exposure to molds, develop permissible exposure limits, and establish practical standards to assess the health risk of indoor molds. The department must also establish guidelines for identification of molds and guidelines for remediation. The Act will not take effect until the first January 1 or July 1 that occurs at least 6 months after the department adopts standards under Health & S C §§26103 and 26105, and guidelines under Health & S C §26130. After the department adopts standards under Health & S C §§26103 and 26105 and develops guidelines under Health & S C §26130, sellers and transferors of commercial and industrial real property must provide written disclosure to prospective buyers, as soon as practicable before the transfer of title, of the presence of mold known to the seller if the mold exceeds permissible exposure limits or poses a health threat. Health & S C §26140(a). The same disclosure must be given to prospective and current tenants of commercial and industrial buildings, occupants of buildings owned by public entities, and tenants of residential properties. Health & S C §§26140-26147. In addition, parties to a lease of commercial or industrial property, whether landlord or tenant, must remediate mold in the building or the HVAC systems and investigate for the presence of mold if there is "a condition of chronic water intrusion or flood." Health & S C §§26143, 26145.

The Act specifically provides that nothing in it will limit existing obligations of parties to a real estate contract to disclose material facts affecting the value and desirability of the property. Health & S C §26150(a). As a result, there appears to be a duty to disclose the existence of molds in a building by a seller even before the department adopts the standards and guidelines referred to in the Act.

The department's obligation to conduct the studies and develop the guidelines envisioned by the Act is unclear. The department must implement the Act only to the extent that it determines there are available funds for such implementation. Health & S C §26156.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.83 G. Financing

§4.83 G. Financing

When a buyer is willing to purchase only if acceptable financing can be obtained, the agreement must be conditioned on the buyer's success in obtaining that financing. The condition must be clearly stated to avoid uncertainty. On uncertainty as a defense, see California Real Property Remedies and Damages §4.19 (2d ed Cal CEB 2002). To avoid uncertainties, the following points should be observed in drafting conditions relating to financing (see section 3.6 of form 4.171-6):

- *Amount.* The buyer should state the minimum loan amount expected. The seller should place a realistic maximum on the amount to be borrowed, especially if taking back a subordinate note.
- *Interest.* Failure to state the interest rate may amount to a fatal uncertainty. The buyer generally states a maximum.
- *Amortization and term of loan.* With the loan amount and interest rate set, the amortization period fixes the term of the loan (unless there is a balloon payment at the end of the term) and the size of the periodic payment. See *Bruggeman v Sokol* (1954) 122 CA2d 876, 265 P2d 575. To avoid ambiguity, the parties should be careful that the periodic payments, duration, amount, and interest rate of the loan are consistent. Loan officers at lending institutions are usually willing to furnish this information. The parties may consider the possibility of an alternative to the conventional fixed-rate note. On amortization, see California Real Estate Finance Practice: Strategies and Forms §§1.74-1.79 (Cal CEB 2000).
- *Penalties and fees.* Loan fees and penalties for prepayment may be costly and should be made part of the condition. Loan fees are often expressed in points. (A "point" is 1 percent of the loan amount, *e.g.,* 5 points on $50,000 is $2500.) The loan fee effectively reduces the amount of new financing the buyer can obtain, whether it is deducted from the loan or paid by the buyer. On points and loan fees, see Real Estate Finance, chap 1.
- *Identity of lender.* Buyers generally prefer to borrow from institutional rather than private lenders and include the condition that the loan is to come from an institutional source. Otherwise, a seller might be able to put the buyer in default by showing that the loan could be obtained from a private source. The seller may seek to limit the choice to a specific type of institutional lender, *e.g.,* banks or insurance companies, or a specific institutional lender. On sources of financing, see Real Estate Finance §§1.17-1.24.
- *Good faith effort.* The requirement, express or implied, of a good faith effort to obtain financing is not satisfied if the buyer unsuccessfully applies to only two banks or fails to apply to a mortgage company after being informed that financing may be available from the latter. *Fry v George Elkins Co.* (1958) 162 CA2d 256, 327 P2d 905. To obviate litigation on whether the buyer satisfied the obligation to seek financing, it may be wise to spell out the precise steps the buyer is expected to take.
- *Time in which to obtain financing.* If no time limit is stated, a reasonable time is implied. CC §1657. Because a "reasonable" time may have to be fixed by litigation, it is generally better to set a time within which the buyer believes the necessary funds can be obtained.
- *Type of commitment required from lender.* The lender or the buyer may require a written loan commitment agreement. On loan commitments, see Real Estate Finance, chap 2.
- *Subordination and release provisions.* If intended subordination and release provisions are not sufficiently specific, the sales agreement may be unenforceable or subject to litigation after the sale is completed. On these provisions, see §§9.66-9.110.

The buyer's financing condition should encompass two provisions: (1) It should waive the buyer's initial contingency to obtain financing (section 3.6 of form 4.171-6) and provide that the deposit will be paid to the seller as liquidated damages on the buyer's default after receipt of a loan commitment (section 9.2 of form 4.177-2), and (2) it should condition the buyer's obligation to close on funding by the lender at closing (section 6.1.5 of form 4.174-1). If the agreement is conditional only on obtaining a commitment rather than on the loan itself, the buyer risks having the lender breach the loan commitment and refuse to close the loan. The buyer would then be in default, and the seller

would have the remedies of the agreement and at law for the default. See *Patterson v Marchese* (1960) 196 NYS2d 903.

Many commitments are subject to numerous conditions, and some lenders breach their commitment when interest rates increase. The loan itself cannot be made until closing, because the buyer must have title to be able to give the required security of a deed of trust. Construction loans usually require that any needed subdivision be completed (see §4.92), necessary use permits be obtained (see §4.87), and building permits be issued. Whether the agreement is conditioned on closing the loan or on obtaining the commitment may be a matter for negotiation, but most buyers cannot take the risk that the loan will not close.

PRACTICE TIP: The seller may wish to limit the buyer to certain types of lending institutions to avoid speculative loans at high interest rates or inflated appraisals. This problem may be controlled to an extent by the interest rates, loan fee, and other agreed terms. The seller may also want assurances that the buyer cannot use the financing condition as an escape provision.

© The Regents of the University of California

§4.84 H. Seller's Books and Records

Many aspects of the operation of income property may seriously affect its attractiveness to the buyer. To analyze past operations of the property, the buyer should review the seller's books and records. The list of documents below is not exhaustive; see the checklist of due diligence materials to be delivered by the seller for a property with commercial leases in App C. The information the buyer should review includes these items:

- Books of account;
- Collective bargaining agreements;
- Employment agreements;
- Equipment or service rental agreements;
- Income statements;
- Installment purchase agreements;
- Insurance policies;
- Warranties on equipment, such as heating and air-conditioning units;
- Guard service contracts;
- Maintenance contracts; and
- Management agreements.

Such an examination may expose items such as an air-conditioning system that needs repeated repairs or other unexpected recurring expenses. The buyer should compare these figures with the data presented by the seller's broker to verify that the assumptions on which the buyer based the offer are correct.

The seller may have contractual arrangements for management, maintenance, security, and similar matters that the buyer will want to examine and have the right to approve or disapprove. Contracts for services to the property and collective bargaining agreements affecting persons employed by the seller should be examined to make sure that such agreements are acceptable to the buyer or cancelable within a reasonable time after the close of escrow. If not, the buyer may wish to have the seller arrange to terminate the agreements or adjust the purchase price.

See section 3.1 of form 4.171-1.

© The Regents of the University of California

I. Use and Development of Property

§4.85 1. In General

The buyer must ascertain that the property is suitable for the intended use. Doing so may require obtaining a study from a space planner or an architect, the results of which may not be apparent when the purchase and sale agreement is signed. One approach is to include a broad approval right in the agreement. Sellers will want to limit the time for giving the approval so that the property is not tied up any longer than necessary. Another approach is to specify the matters the buyer must approve, narrowing the scope of the buyer's discretion. To further limit the buyer, the seller could require the buyer to provide the seller with a copy of the opinions from the listed professional advisers that support the buyer's termination of the agreement.

PRACTICE TIP: When drafting a purchase agreement for a development project, buyer's counsel should take care not to draft a "disguised option" that may fail for lack of consideration. In *Steiner v Thexton* (review granted Sept. 17, 2008, S164928; superseded opinion at 163 CA4th 359, 77 CR3d 632), the court of appeal held that a purchase contract allowing the buyer, in its sole discretion, to terminate the contract if certain entitlements were not obtained was not an enforceable contract but a "continuing offer to sell," which could be revoked by the seller at any time. The court dismissed the buyer's argument that the $60,000 spent to obtain a parcel split was sufficient consideration. For further discussion, see 31 CEB Real Prop L Rep 117 (July 2008). The California Supreme Court has granted review of *Steiner*.

© The Regents of the University of California

§4.86 2. Zoning

Zoning can be crucial to the property's value to the buyer. The buyer should confirm the zoning before waiving its conditions to closing and should confirm that the proposed sale will not affect the zoning or proposed zoning.

If the present zoning appears to permit the intended use of the property, the buyer should make confirmation of the zoning with the zoning authorities a condition of closing and should attempt to obtain a warranty from the seller. See buyer-oriented seller's representations and warranties in form 4.173-1, Alternative 1, section 5.1.2. Sellers usually resist any such warranty, however, leaving the buyer to ascertain what zoning and other governmental approvals are required for the intended use.

Sometimes the buyer's plans for the property will require a change in the zoning or land use designation. Because the property will be of little value to the buyer without a change, the buyer will want to obtain the change before risking its deposit. A change can be obtained in one of three ways:

- By amendment to the zoning ordinance;
- By a variance from current zoning; or
- By a conditional use permit.

On the distinctions among these devices and zoning generally, see California Land Use Practice, chap 7 (Cal CEB 2006). Note that even a change in zoning will not give the buyer a vested right to develop the property in accordance with the change. In general, a landowner acquires a vested right in zoning only by obtaining a building permit and, relying on the permit, by incurring obligations or expending funds for actual on-site improvements. *Avco Community Developers, Inc. v South Coast Regional Comm'n* (1976) 17 C3d 785, 132 CR 386; *Raley v California Tahoe Regional Planning Agency* (1977) 68 CA3d 965, 137 CR 699. Under the Development Agreements Law (Govt C §§65864-65869.5), however, a landowner can preserve existing zoning for a period of time by entering into a development agreement with the city or county in which the land is located. See also *Santa Margarita Area Residents Together v San Luis Obispo County Bd. of Supervisors* (2000) 84 CA4th 221, 100 CR2d 740; §1.89. On development agreements, see California Subdivision Map Act and the Development Process, chap 7 (2d ed Cal CEB 2001).

PRACTICE TIP: The seller may not wish to have the zoning changed if the sale does not close. To limit the chances of being bound by an unwanted change, the seller may require that the applications for the change be worded so that the change will not occur if the sale does not close.

The buyer's commitment to file documents and pay fees fortifies the element of mutuality discussed in §4.3. If time expires before a rezoning determination is made or if the determination is adverse, the agreement can give the buyer an option to cancel or waive the condition. This option is more favorable to a buyer than is automatic termination. See *Isaacson v G. D. Robertson & Co.* (1948) 85 CA2d 71, 192 P2d 486, in which an automatic termination provision prevented the buyer from waiving the benefit of a zoning provision.

In connection with the rezoning, a seller-oriented provision would

- require the buyer to file the rezoning application within a certain number of days after execution of the agreement;
- impose a time limit on each step of the proceeding;
- eliminate the buyer's unilateral right to extend the closing; and
- provide for automatic cancellation of the agreement if the buyer fails to rezone within the stated time period.

Zoning ordinance amendments are considered legislative in nature and must be made by an ordinance approved by the local legislative body. A proposal to adopt a zoning amendment triggers the California Environmental Quality Act (CEQA). Pub Res C §21080. See §§4.94-4.98. On CEQA generally, see Practice Under the California Environmental Quality Act (2d ed Cal CEB 2008). Amendments to zoning laws follow the same procedures as adoption of zoning ordinances (Govt C §65853), *i.e.,* the planning commission must hold a noticed public hearing and submit a recommendation to the legislative body (Govt C §§65854-65855). See *People v County of Kern* (1974) 39 CA3d 830,

115 CR 67. The legislative body must usually hold a hearing as well. Govt C §§65855-65856. In addition, cities and counties are required to amend their zoning ordinances as they become inconsistent with the applicable general plan, and the amendments must be made within a reasonable time. Govt C §65860(c). See Higginbotham, *The Compatibility of Economic and Environmental Objectives in Governmental Decision Making*, 5 Pac LJ 92 (1974). Because a rezoning determination is made by ordinance, there is a 30-day referendum period during which the decision can be challenged. Elec C §§9141, 9144 (counties), 9235, 9237 (cities).

Zoning changes in recent years have tended to increase the nature and extent of regulations. Other bases for zoning, such as esthetics or local economic considerations, raise new risks of future zoning changes. See *Bohannan v City of San Diego* (1973) 30 CA3d 416, 106 CR 333; *Van Sicklen v Browne* (1971) 15 CA3d 122, 92 CR 786; *Burk v Municipal Court* (1964) 229 CA2d 696, 40 CR 425. See also *Hernandez v City of Hanford* (2007) 41 C4th 279, 59 CR3d 442 (disapproving inconsistent language of *Van Sicklen* and clarifying use of "economic considerations" in zoning determinations).

Local planning maps and general plans contain information on projected changes but do not ensure that no other changes will occur, as noted above. The purchase of property for a valid consideration does not confer on the buyer a vested right in present zoning or against future moratoriums or changes in zoning. *Avco Community Developers, Inc. v South Coast Regional Comm'n, supra*; *Morse v County of San Luis Obispo* (1967) 247 CA2d 600, 55 CR 710. For a detailed discussion of vested rights and the *Avco* decision, see California Land Use Practice, chap 16 (Cal CEB 2006).

© The Regents of the University of California

§4.87 3. Conditional Use Permits and Variances

On a proper showing, existing zoning restrictions may be modified by variances or conditional use permits. On the distinction between the two, see *Van Sicklen v Browne* (1971) 15 CA3d 122, 92 CR 786, and *Tustin Heights Ass'n v Board of Supervisors* (1959) 170 CA2d 619, 339 P2d 914. Both are issuable, not as a matter of right but as a matter of grace, within the discretionary power of the granting authority. *Tustin Heights Ass'n v Board of Supervisors, supra*. See also California Land Use Practice, chap 7 (Cal CEB 2006).

Conditional use permits are provided for in most zoning ordinances. Typically, such permits provide a way to allow different uses to coexist in a zone on a decision by the appropriate zoning body that the use for which the permit is sought will not be inconsistent with public health, morals, safety, or welfare. This permit is administrative in nature, but it differs from a variance in that it allows uses that are only conditionally permitted under the zoning ordinance. See, *e.g., Essick v City of Los Angeles* (1950) 34 C2d 614, 213 P2d 492. Under Govt C §65901, either the board of zoning adjustment or a zoning administrator must hear and decide applications for such permits. See California Land Use Practice §§7.10-7.21 (Cal CEB 2006).

In general, variances can be granted only when, because of special circumstances applicable to the particular property (*e.g.,* size, topography, location, shape), strict application of the zoning ordinance would unfairly deprive the subject property of the same privileges enjoyed by other properties in the area that are subject to identical zoning classifications. Govt C §65906. Granting a variance for a use or an activity that is not otherwise authorized by the zoning ordinance is prohibited by §65906 (which apparently does not apply to charter cities). The requirement that special circumstances be shown has led to substantial litigation over the years regarding the approval or denial of variances. See, *e.g., Broadway, Laguna, Vallejo Ass'n v Board of Permit Appeals* (1967) 66 C2d 767, 59 CR 146; *Siller v Board of Supervisors* (1962) 58 C2d 479, 25 CR 73; *Zakessian v City of Sausalito* (1972) 28 CA3d 794, 105 CR 105; *Hamilton v Board of Supervisors* (1969) 269 CA2d 64, 75 CR 106.

It is now clear that the special circumstances claimed to justify the variance must be such that they make the property different from other property in the same zone. *Topanga Ass'n for a Scenic Community v County of Los Angeles* (1974) 11 C3d 506, 113 CR 836. Because the statutory standards for a variance require that the strict application of the zoning ordinance would deprive the property of privileges enjoyed by other properties in the same area with the same zoning classification, the court must find that unnecessary hardship would be created if a variance were not granted. See *Zakessian v City of Sausalito, supra*.

On variances generally, see California Land Use Practice §§7.2-7.9.

© The Regents of the University of California

§4.88 4. Coastal Development Permits

Coastal development permits may be required for any improvement or modification of property within the coastal zone. California Coastal Act (Pub Res C §§30000-30900). The coastal zone extends seaward to the state's jurisdictional limit, includes all offshore islands, and generally extends inland 1000 yards from the mean high tide line. In certain coastal estuarine, habitational, or recreational areas, it may extend up to 5 miles inland. Pub Res C §30103. If the property is within 5 miles of the shoreline, a prospective buyer should check the map on file with the county clerk to ascertain whether the property falls within the coastal zone. If so, development of the property will be subject to stringent controls under the Act. For example, in *California Coastal Comm'n v Quanta Inv. Corp.* (1980) 113 CA3d 579, 609, 170 CR 263, the court held that the conversion of an apartment building in the coastal zone into a stock cooperative was subject to the permit requirements of the California Coastal Commission.

PRACTICE TIP: To be assured that the property can be developed, the buyer should insist that closing be conditioned on issuance of a coastal development permit, approval of any conditions in it, and expiration of the time to challenge the permit.

If there is an existing coastal development permit, it is assignable under the procedures in 14 Cal Code Regs §13170, which requires the original permittee's submittal of a request for assignment. The buyer should obligate the seller to cooperate in transferring the permit. For further discussion of the California Coastal Act, see California Land Use Practice, chap 14 (Cal CEB 2006).

© The Regents of the University of California

§4.89 5. Other Permits

If the buyer's use of the property depends on obtaining a governmental approval, such as a liquor license or a building permit, the buyer will want to obtain it before close of escrow. Issuance of a permit or license does not guarantee that the buyer will be able to develop the property as planned, however, nor does issuance of a building permit vest a buyer's right to build the improvements for which it was issued. The buyer must be able to show detrimental reliance on the permit for the rights to vest. A permit holder without a vested right is subject to any change in the law, including a change made after the date of the permit. See discussion in §4.86. Even if the buyer's rights vest, they are limited to the terms and conditions of the permit and do not go beyond the project described in the approval.

Usually, obtaining a permit is as far as a buyer can go during escrow because sellers generally do not allow a buyer to commence construction before the close of escrow.

Often, governmental agencies require the property owner to sign any applications for governmental permits or changes of the status of the property, such as rezoning or subdivision applications. A buyer who wishes to learn whether the permits and other governmental actions required for the project are obtainable before the close of escrow therefore needs the seller's cooperation. The seller, however, must be certain that no change that might affect future development of the property becomes final before the close of escrow, in the event the transaction does not then close.

© The Regents of the University of California

§4.90 6. Access

The buyer should review what access to the property is needed to accomplish the purchaser's intended use of the property. If the property is to be used for commercial purposes, access is crucial. The buyer should check the ease of entry to and exit from the property and the capacity and traffic flow of nearby streets. The buyer should also check with local officials to learn whether there are any plans to improve, change, or abandon adjacent streets.

EXAMPLE: The addition of a median in a street can have a significant impact on a commercial development because access from one direction is cut off or limited to specific openings in the divider.

The buyer should also check access from nearby major traffic arteries. Traffic planners generally limit the number of curb cuts for access in an attempt to avoid impairing the traffic flow by cars entering at many points along the highway. Such limitations may or may not be compatible with the buyer's intended use.

Even if the property's intended use is not commercial, the buyer should make sure that access to the property is adequate. If local governmental requirements on emergency access are not complied with, a building permit may be denied.

On title insurance products that cover access, see California Title Insurance Practice §§6.27, 7.13, 7.72-7.73, 8.59-8.60 (2d ed Cal CEB 1997).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.91 7. Annexation

§4.91 7. Annexation

When the property is in an unincorporated area, its annexation to a city is often essential to a buyer who wants to be certain that services are available for the intended use. In some counties, water, sewer, and other services are provided by special districts to which the property must be annexed in order to obtain the services.

Annexation is governed by the Cortese-Knox-Hertzberg Local Government Reorganization Act of 2000 (Govt C §§56000-57550) and is subject to the powers of the Local Agency Formation Commission (LAFCO). One purpose of LAFCOs is to discourage urban sprawl and encourage the orderly formation and development of local agencies based on local conditions and circumstances. Govt C §56301.

LAFCO proceedings for annexations may be initiated by petition by 5 percent of registered voters in the territory to be annexed or resolution of the city wishing to annex. Govt C §§56650, 56755(a). Petition requirements are in Govt C §§56700-56711; signature requirements for petitions are in Govt C §§56750-56762. A LAFCO itself may initiate proposals in certain circumstances. Factors a LAFCO must consider in initiating or reviewing proposals are specified in Govt C §56375. A LAFCO cannot disapprove the annexation of territory surrounded or substantially surrounded by a city if certain conditions are met. See Govt C §56375(a).

The seller may be liable for unpaid annexation fees if the buyer defaults after annexation has begun. The buyer may find that additional conditions to annexation require the annexing party to finance new or parallel facilities (such as pipelines), to pay a retroactive prorata share of taxes, or to otherwise share in the city's or district's financial burdens.

PRACTICE TIP: Because annexation conditions vary widely, the buyer's attorney should confer with the executive officer of the LAFCO and the city attorney or district counsel, before negotiating the purchase agreement, to ascertain the scope and nature of conditions likely to be imposed.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.92 8. Subdivision

§4.92 8. Subdivision

The buyer should confirm that the property as it is being sold complies with the Subdivision Map Act (Govt C §§66410-66499.37). The Act requires a final subdivision map or a parcel map for any division of land. A sale, lease, or encumbrance of only a portion of a larger parcel triggers application of the Act. Govt C §66499.30. If the property is described by a lot number on a recorded final map or parcel map, it presumably conforms to the Act. Govt C §66499.35(a), (d). If the property is described in any other manner, further investigation is required to ascertain whether the property conforms to the Act.

Under Govt C §66424, "subdivision" is defined to mean

> the division, by any subdivider, of any unit or units of improved or unimproved land, or any portion thereof, shown on the latest equalized county assessment roll as a unit or as contiguous units, for the purpose of sale, lease or financing, whether immediate or future.

Government Code §66412 lists the exclusions to the term "subdivision."

A sale, lease, or financing of real property that has not been divided in accordance with the Subdivision Map Act is prohibited unless the owner first records a final map or parcel map. Govt C §66499.30(a)-(b). A contract for sale, lease, financing, or construction that is expressly conditioned on the approval and filing of a final subdivision map or parcel map is permitted. Govt C §66499.30(e). However, this condition cannot be waived. A contract for the purchase and sale of real property is void at inception if the contract allows the buyer to complete the purchase when a final map is recorded, or waive the recording of the final map. *Sixells, LLC v Cannery Bus. Park* (2008) 170 CA4th 648, 88 CR3d 235. See also *Black Hills Invs., Inc. v Albertson's, Inc*. (2007) 146 CA4th 883, 53 CR3d 263. On the Subdivision Map Act generally, see California Subdivision Map Act and the Development Process (2d ed Cal CEB 2001).

If the seller has not complied with the Act, the buyer may void the transaction or sue for damages within 1 year after discovering the violation (Govt C §66499.32), and local agencies are barred from issuing any permit or granting any approval necessary to develop the property (Govt C §66499.34). Failure to comply with the Act does not render title unmarketable, however, and a buyer probably has no right of recovery under a standard title insurance policy (*Nishiyama v Safeco Title Ins. Co.* (1978) 85 CA3d Supp 1, 149 CR 355), unless the buyer has obtained a subdivision endorsement for its title insurance policy. See also California Title Insurance Practice §§6.23-6.25, 6.38, 11.71-11.72 (2d ed Cal CEB 1997).

If the parties believe that the property is in compliance with the Act but wish to confirm its compliance, they may obtain a Certificate of Compliance under Govt C §66499.35(c) from the local agency that approves maps. The procedures for issuing certificates vary from one jurisdiction to another. Title companies will also issue an endorsement confirming that the property complies with the Act. If compliance may be questioned, this endorsement can be a good investment. See Title Ins §7.95.

When land is purchased for subdivision, the buyer usually wants an assurance that the appropriate governmental agency will approve a subdivision map permitting development. Under the Act, cities and counties have the power to regulate and control the design and improvement of subdivisions, and each city or county must adopt an ordinance regulating and controlling subdivisions whenever state law requires a tentative, final, or parcel map. Govt C §§66411-66411.1. See *Friends of Lake Arrowhead v Board of Supervisors* (1974) 38 CA3d 497, 113 CR 539, on local supplemental ordinances.

The terms "design" and "improvement," which are the elements of subdivisions that may be regulated by cities and counties, are defined broadly. For example, "design" includes street alignments, grades and widths, drainage and sanitary facilities, easements and rights of way, fire roads, lot size and configuration, access, grading, land to be dedicated for park or recreational purposes, and any other specific requirements that are "necessary or convenient" to ensure conformity to or implementation of the local agency's general plan or any adopted specific plan. "Improvement" includes street work and utilities to be installed by the subdivider, highways, easements, and any other specific improvements or types of improvements whose installation is necessary or convenient to ensure conformity to or implementation of the local agency's general or specific plans. Govt C §§66418-66419. See Subdiv Map Act §5.26; 9

Miller & Starr, California Real Estate, chap 25 (3d ed 2000).

Like other conditions to the agreement, delaying execution of the agreement until approval is obtained requires the buyer to spend money and the seller to withhold the property from the market without assurance to either party that an agreement will eventually be signed. Conditioning the agreement on the governmental agency's approval of a subdivision map acceptable to the buyer permits the buyer to seek that approval before completing the purchase. In general, the buyer may not unreasonably withhold acceptance of the approved map. *Rodriguez v Barnett* (1959) 52 C2d 154, 338 P2d 907. In practice, agreements often give buyers wide discretion and state minimum numbers of lots, lot sizes, and other conditions that must be met before a buyer will approve a subdivision map. Obtaining approval of a subdivision map is often very time consuming, and the seller may not be willing to wait. On the other hand, the purchase price of the property may be justified in the minds of both parties only after the subdivision is approved. For use of options, see chap 8.

© The Regents of the University of California

§4.93 9. Williamson Act

The buyer needs to determine whether the property's use is restricted by the California Land Conservation Act of 1965 (Williamson Act) (Govt C §§51200-51297.4), which provides for the establishment of agricultural preserves and the formation of long-term contracts between landowners and local governments to restrict the use of agricultural land to agricultural or compatible uses. Land so restricted is assessed for tax purposes according to its restricted use rather than its development potential free of such restriction. Govt C §51252; Rev & T C §§421-430.5. See also Cal Const art XIII, §8.

With certain exceptions, Govt C §66474.4 requires that an application for a tentative map or parcel map must be denied if the local government finds that the land is subject to a Williamson Act contract and either (1) the resulting parcels following subdivision would be too small to sustain their agricultural use, or (2) the subdivision will result in residential development not incidental to the commercial agricultural use of the land. (For discussion of this provision, see California Subdivision Map Act and the Development Process §9.31 (2d ed Cal CEB 2001).) In some cases, it may be necessary to seek cancellation of the Williamson Act contract before the subdivision can be approved. If written notice of the contract's nonrenewal has been served and the contract will expire within 3 years, the subdivision prohibitions do not apply. See Govt C §66474.4(f).

NOTE: State reimbursements to counties for Williamson Act incentives were eliminated by line item veto in the California state budget for fiscal year 2009-2010. For a website on the state budget, see Directory. Existing contracts remain valid, but lawyers and their clients may wish to assess the probability of the renewal of existing contracts and/or new contracts in the current budgetary environment.

For a discussion of the requirements for canceling Williamson Act contracts, see California Subdivision Map Act and the Development Process, chap 4 (2d ed Cal CEB 2001).

© The Regents of the University of California

§4.94 10. California Environmental Quality Act

The California Environmental Quality Act (CEQA) (Pub Res C §§21000-21177) was enacted in 1970 to enhance the environmental quality of the state by requiring all governmental agencies to consider qualitative factors and long-term benefits and costs as well as economic and technical factors in connection with proposed projects that the agency intends to carry out or approve. Pub Res C §§21000-21001. Government agencies are barred from approving a project as proposed if feasible alternatives or mitigating measures would substantially reduce the project's adverse environmental effects. If specific economic, social, or other conditions make a proposed alternative infeasible, however, an agency may approve the project as originally proposed. Pub Res C §21002.

On CEQA generally, see Practice Under the California Environmental Quality Act (2d ed Cal CEB 2008).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.95 a. Requirement for Environmental Review

§4.95 a. Requirement for Environmental Review

All state and local agencies must review the environmental impact of any project they propose to carry out or approve that may have a significant effect on the environment. Pub Res C §§21100, 21151.

A "project" is an activity that may cause a direct physical change, or a reasonably foreseeable indirect change, in the environment and that (Pub Res C §21065)

- is directly undertaken by any public agency;
- is supported in whole or in part through contracts, grants, subsidies, loans, or other forms of assistance from one or more public agencies; and
- involves the discretionary issuance of a lease, permit, license, certificate, or other entitlement for use by a public agency.

Only projects that entail an exercise of discretion or judgment by the agency require an Environmental Impact Report (EIR). CEQA does not apply to ministerial acts. Pub Res C §21080; 14 Cal Code Regs §15300.1. Ministerial acts include acts required by law on the occurrence of a certain contingency, such as issuance of a building permit or a business license, approval of a final subdivision map, or a utility connection or disconnection. 14 Cal Code Regs §15268. The issuance of a grading permit is not a ministerial act (*Day v City of Glendale* (1975) 51 CA3d 817, 124 CR 569), nor is the enactment of a rezoning ordinance (56 Ops Cal Atty Gen 404 (1973)).

"Significant effect on the environment" means a substantial or potentially substantial change in the physical conditions in the area that will be affected by the proposed project, including land, air, water, minerals, flora, fauna, ambient noise, and objects of historic or esthetic significance. Pub Res C §§21060.5, 21068.

Whether a project will have a significant effect on the environment is a question of fact that depends on many factors, some of which are listed in 14 Cal Code Regs Div 6, chap 3, App G (environmental checklist). The courts have held that an EIR should be prepared whenever an agency perceives "substantial evidence that the project may have a significant effect environmentally" or that the project "arguably will have an adverse environmental impact." *No Oil, Inc. v City of Los Angeles* (1974) 13 C3d 68, 85, 118 CR 34. "Substantial evidence" is now defined to include "fact, a reasonable assumption predicated upon fact, or expert opinion supported by fact." Pub Res C §21080(e)(1). On whether a project will have a significant impact on the environment, see Practice Under the California Environmental Quality Act, chap 6 (2d ed Cal CEB 2008).

Local agencies are required to complete the EIR within 1 year after the date that an application requesting approval of a project is filed and accepted as complete. Pub Res C §21151.5(a). See also *Sunset Drive Corp. v City of Redlands* (1999) 73 CA4th 215, 86 CR2d 209.

© The Regents of the University of California

§4.96 b. Exemptions and Negative Declarations

If a project that requires a discretionary governmental approval may have a significant effect on the environment, it will require study under CEQA. Such a study does not necessarily mean that an Environmental Impact Report (EIR) will be required. Before an EIR is begun, the agency conducts an "initial study" to decide whether it is required. No EIR is required if the agency issues (1) a notice of exemption because the property is statutorily exempt from CEQA (Pub Res C §§21080(b), 21080.01-21080.33; 14 Cal Code Regs §§15260-15285) or categorically exempt (14 Cal Code Regs §§15300-15333); (2) a negative declaration because it finds that the project will have no significant effect on the environment (14 Cal Code Regs §§15070-15075); or (3) a mitigated negative declaration because the initial study (14 Cal Code Regs §§15060-15065) identified potentially significant effects on the environment but revisions in the plans or proposals would avoid or mitigate them and there is no substantial evidence that the project, as revised, may have a significant effect on the environment (Pub Res C §21064.5). See Practice Under the California Environmental Quality Act, chap 7 (2d ed Cal CEB 2008).

© The Regents of the University of California

§4.97 c. Environmental Impact Reports (EIRs)

If the project is not exempt and potential significant effects on the environment cannot be mitigated, an Environmental Impact Report (EIR) must be prepared. Preparation of an EIR must be considered at a very early stage in development planning. An EIR is required to focus on potential effects on the environment that the lead agency has determined are, or may be, significant and may limit the discussion of other effects to a brief explanation of why they are not potentially significant. Pub Res C §21002.1(e). See Practice Under the California Environmental Quality Act, chaps 8-16 (2d ed Cal CEB 2008).

© The Regents of the University of California

§4.98 d. Impact on Buyer

If an Environmental Impact Report (EIR) may be required for a project, counsel should review the case law and Title 14 of the California Code of Regulations on interpreting and implementing CEQA. If it appears that CEQA will require some study of the project, counsel should discuss with the buyer the potential costs and delays. The buyer may not wish to proceed with the purchase without an assurance that the project can be built. An option to buy or a long escrow period may be agreed on to allow the buyer time to comply with the EIR process and obtain an agency ruling on the project before committing to purchase the property. The buyer should remember that obtaining governmental approvals does not guarantee a right to develop, because the approval of an EIR, issuance of a negative declaration (mitigated or not), and a determination that the project is exempt are all subject to a court challenge by any persons who feel they will be harmed by the project.

NOTE: Under CEQA, if a notice of determination is properly filed by the agency after its decision, a short statute of limitations (usually 30 days) applies to actions challenging the decision. Pub Res C §§21108, 21167; 14 Cal Code Regs §15075. Courts are to give preference to actions brought under CEQA, and superior courts in counties with populations of more than 200,000 are to designate one or more judges to develop expertise in CEQA, related land use, and environmental laws. Pub Res C §21167.1.

© The Regents of the University of California

J. Failure to Meet Due Diligence Conditions

§4.99 1. Issues Regarding Failure of Conditions

When the buyer objects to the title, physical condition, or use of the property within the approval period, several questions arise, and the agreement should be clear on each point:

- Does the objection terminate the agreement automatically, or does it give the buyer an option to terminate? An automatic termination provision limits each party's flexibility and should be carefully considered before including it. If the agreement does not provide for automatic termination, the party for whose benefit the condition exists may be given an election to waive the defect. See section 6.3 of form 4.174-3 for a provision permitting termination but not requiring automatic termination.
- Does the agreement give one party an obligation or election to cure the defect? For a provision obligating the seller to remove monetary defects in title, see section 3.4.2 of form 4.171-4. For provisions giving the seller an election to remove other title defects (except buyer's failure to obtain financing), see section 3.4.4 of form 4.171-4.
- If the defect cannot be cured, what course of action is open to each party? See section 3.4.3 of form 4.171-4, which gives the buyer the option to waive the defect and purchase the property or terminate the agreement.
- If the agreement is terminated, how is the buyer's deposit returned? See discussion of recovery of buyer's deposit in §4.100.

The same questions should be asked if the condition is for the seller's benefit.

© The Regents of the University of California

§4.100 2. Recovery of Buyer's Deposit

If the agreement and the escrow, if any, are to be canceled because of the buyer's disapproval of some item or failure of performance of some condition, the buyer's primary concern is the speedy return of the deposit or downpayment. Thus, the agreement should normally provide for repayment to the buyer, which is more readily achieved if the deposit or downpayment was placed in escrow rather than delivered to the seller or its broker. A repayment provision might not operate effectively in practice, however. If a dispute arises, the escrow holder may be unwilling to release the funds without both parties' cancellation instructions (signed after the cancellation) and may interplead the funds, creating an unfavorable situation for the buyer. On the interpleader of disputed funds by the escrow holder, see §15.98.

PRACTICE TIP: To avoid the possibility that a dispute will prevent or delay a refund to the buyer when an agreement is canceled for failure of a condition, the buyer should attempt to make a minimal deposit at the time of executing an agreement (perhaps just enough to cover costs), and make a more substantial deposit when the agreement's conditions are approved. This arrangement postpones the buyer's outlay of funds until the agreement becomes unconditional, and it protects the buyer from having funds tied up in a disputed escrow. See form 4.170-2.

If, in addition to getting the deposit back, the buyer wishes to reserve the right to damages (if a covenant was breached) or specific performance, the buyer should attempt to make this right explicit in the agreement (although a seller would rarely agree to this). Otherwise, the return of the deposit may be interpreted as terminating the agreement. See California Real Property Remedies and Damages §§4.32-4.38 (2d ed Cal CEB 2002). If the agreement is considered terminated, the buyer is prevented from waiving the defect and buying at a reduced price. See also *Beverly Way Assocs. v Barham* (1990) 226 CA3d 49, 276 CR 240, in which the buyer disapproved some reports and made proposals for restructuring the transaction. After receiving no response from the seller, the buyer wrote to the seller 60 days later, waiving its objections and offering to complete the purchase. The seller canceled the escrow, and the buyer sued for specific performance. The court held that the buyer's letter disapproving the reports had terminated the contract. To avoid such a result, some agreements expressly reserve the buyer's right to waive the defect and buy at a reduced price.

Under CC §1057.3, if a party wrongfully fails to execute the documents necessary to release a deposit after an escrow fails to close by the date specified in the escrow instructions, the injured party can recover the deposit plus a penalty of three times the deposit (at least $100 but no more than $1000) plus attorney fees. The penalty does not apply if the funds are withheld to resolve a good faith dispute. The statute applies only to residential one-to-four-unit property that the buyer intends to occupy.

© The Regents of the University of California

VII. COVENANTS PENDING CLOSING

A. Leases

§4.101 1. Covenant by Seller to Obtain Estoppel Certificates

In addition to a closing condition requiring the seller to deliver estoppel certificates signed by the tenants of the property being purchased (see §4.73 and section 6.1.4 of form 4.174-1), some buyers also request that the seller covenant to obtain the estoppel certificates (see section 4.10 of form 4.172-10). The reason for the covenant is to make available a claim for damages if the certificates are not delivered, and therefore many sellers resist such a request. One compromise requires the seller to provide seller's certificates representing and warranting the information that would have been provided in the estoppel certificates not delivered by tenants. The result is that the seller guarantees the leases. Sellers then endeavor to obtain estoppel certificates from the tenants, continuing this effort after closing. For sample estoppel certificate, see App K.

© The Regents of the University of California

§4.102 2. Limitations on New Leases

The buyer does not want to be bound by a last-minute lease negotiated by the seller, but may also not want to lose either existing tenants who wish to renew their leases or prospective new tenants. Agreements often provide that the seller may enter into new or renewal leases, but the buyer must approve the lease in writing. The seller might also limit the buyer's veto by requiring that it be exercised within a certain number of days after receiving the proposed lease and that the buyer's silence is deemed to be approval. *Louison v Yohanan* (1981) 117 CA3d 258, 172 CR 602, is an example of a successful suit for damages for breach of a purchase contract clause providing that no changes would be made in existing leases. See form 4.172-1.

© The Regents of the University of California

§4.103 3. Seller's Obligation to Terminate Leases

A buyer who is spending material sums of money or making other arrangements in reliance on termination of existing leases at closing may wish to add a covenant that, no later than a certain number of days (*e.g.*, 15) before closing, the seller must obtain agreements from the tenants under which the tenants agree to terminate the leases at closing and add a condition to closing that such agreements be obtained. These provisions give the buyer both a remedy of damages for the seller's breach if such agreements are not obtained and a remedy against the tenants if the leases are not terminated or the tenants do not vacate the premises in a timely manner. See discussion in §4.72.

© The Regents of the University of California

§4.104 B. Seller's Operations of Property

When income property is being purchased, such as office and apartment buildings and shopping centers, the economics of the operation can be as important as the physical condition of the property. The buyer may require that the seller continue to collect rent and otherwise continue to operate in the manner that gave the property its value to the buyer. The seller is usually obligated to maintain the property until the sale closes. See form 4.172-3.

Existing agreements (*e.g.,* management and maintenance agreements) may include provisions that they are binding on heirs, successors, and assigns of the owner. Because buyers usually want to make their own arrangements for the property's maintenance and security, the seller should agree to terminate existing agreements before close of escrow at the buyer's request, even though the buyer does not then become the seller's "successor or assign" in buying the property. The seller may, however, be reluctant to terminate contracts until immediately before the close of escrow because of the possibility that other closing conditions may not be satisfied or that the buyer may default. See form 4.172-11.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.105 C. Seller's Construction Covenants

§4.105 C. Seller's Construction Covenants

It is not unusual for the seller to agree to complete construction of a building or other work in connection with the transaction. If the work is to be done before closing, several conditions should be met, including the following:

- Receipt of the architect's certificate that the project is complete;
- Recordation of a Notice of Completion of the work;
- Confirmation that the final payment was made to the contractor;
- Receipt of a Certificate of Occupancy or its equivalent from the local governmental authority confirming that work under the building permit was completed; and
- Confirmation that the property is free of liens and that the contractor and all subcontractors have supplied lien releases.

PRACTICE TIP: If the seller will complete work after closing, in addition to the matters mentioned above the buyer may want to put part of the purchase price in escrow, pending completion, and may ask for a payment or a performance bond. The buyer and seller must negotiate which party will control the work. This also applies to tenant improvements under construction by the seller at the time of closing, the completion cost of which should be included in the costs and expenses prorated at closing. See §4.133.

© The Regents of the University of California

§4.106 D. Insurance

It is important that the parties understand how the insurance on the property is to be handled. First, the seller should covenant to maintain all existing insurance until closing. The maintenance of hazard insurance must be coordinated with the casualty provisions in the agreement. See §4.137 and form 4.172-2. Second, it must be decided whether any insurance will be transferred to the buyer; if so, the costs will need to be prorated in escrow. Usually, hazard insurance can be transferred directly to the buyer. A transfer of liability insurance may be more difficult, especially if the buyer's intended use of the property differs from the seller's, and is rarely done. Transferring insurance is easier if the property is income property and the same tenants remain in possession, because the insurer's risk is not changed.

If the seller has a blanket policy covering the property being sold and other properties, a transfer may not be possible. If the seller does not object to transferring the insurance, the assumption provision gives the buyer the option of assuming the seller's insurance or obtaining its own. The buyer should be required to allow a sufficient number of days before the closing to permit the insurance agent to handle the paperwork. If the borrower is getting a loan, the lender will not fund the loan until it is satisfied that the property has adequate hazard insurance. If the seller is taking back a note for part of the purchase price, the agreement should set forth the seller's insurance requirements. See chap 13 on property insurance generally.

© The Regents of the University of California

VIII. REPRESENTATIONS AND WARRANTIES

§4.107 A. Purpose

A warranty or representation is an affirmation by the seller of a fact or facts relating to the property. See generally 4 Witkin, Summary of California Law, *Sales* §§51-78 (10th ed 2005). Failure of a condition in the agreement generally excuses a party's performance, but breach of a warranty entitles a party to damages and possibly rescission. Unless a warranty is also a condition, its breach will not relieve the buyer from the duty to perform, although any damages might be offset against any sums owed by the buyer. See 1 Witkin, Summary, *Contracts* §§776-778. The purpose of warranties is to force the seller's full disclosure and provide assurances to the buyer on the property's status or condition. Warranties are often heavily negotiated because the parties have competing objectives: The buyer wants protection from unknown risks, while the seller wants to eliminate warranties or at least limit them to necessary disclosures. If the purchase price is low, or if the buyer negotiated a substantial time period in which to conduct a due diligence investigation, the seller may be unwilling to give more than minimal warranties. For a buyer's form of seller's warranties and representations, see form 4.173-1, Alternative 1; for a seller's form of seller's warranties and representations, see form 4.173-1, Alternative 2.

In a major acquisition, the buyer should request at least the following warranties from the seller:

- There is no litigation arising from or affecting the property;
- There are no known violations of codes or other regulations and no pending zoning changes;
- The seller has disclosed to the buyer all leases, amendments to leases, building service contracts, and similar documents affecting the property;
- There is no violation of any hazardous materials laws; and
- The seller is authorized to enter into the agreement.

Representations and warranties are very negotiable. The extent to which a buyer can obtain extensive warranties or a seller can resist a buyer's demands depends, of course, on the market for properties like the one in question at that particular time. In periods of high demand, sellers can often resist giving extensive warranties.

© The Regents of the University of California

§4.108 B. Limitations on Warranties

A warranty can take different forms, based on the standard of knowledge to which the seller will be held:

- An absolute warranty has no limitation.
- A warranty made "to the best of seller's knowledge" includes what the seller actually knows plus what he or she should have known after a reasonable investigation.
- A warranty of the seller's "actual knowledge" includes only matters that the seller actually knows. It does not include matters that the seller might suspect or that, after reasonable investigation, could be learned.

PRACTICE TIP: A seller may want to limit the "actual knowledge" warranty to matters on which he or she has received written notice, such as threatened condemnation or notice of required seismic work. The seller may further limit this actual knowledge warranty by indicating that it means the knowledge of specified persons only, and that the actual knowledge of the seller (or a specified person) does not require any investigation or inquiry. This limitation is especially desirable when the seller is a large organization such as a bank; it may also benefit the buyer, who is thus informed of the knowledge of key persons. See form 4.173-1, Alternative 2, section 5.1.8, for a definition of "seller's knowledge."

© The Regents of the University of California

§4.109 C. Survival of Warranties

Absent fraud, mistake, agreement, or other special circumstances, the buyer's acceptance of the deed at closing results in a merger of prior negotiations and agreements, and discharges the seller's obligations. The buyer's rights are then measured solely by the deed. *Bryan v Swain* (1880) 56 C 616; *Burnand v Nowell* (1948) 84 CA2d 1, 189 P2d 796. Both of these cases appear to be based on the buyer's intent in accepting the deed. However, matters collateral to the conveyance (*i.e.,* those that ordinarily do not become part of the deed) are not merged (*Stiles v Bodkin* (1941) 43 CA2d 839, 111 P2d 675 (agreement to put in streets)) and, because they survive, may sometimes support an action for damages (*Christensen v Slawter* (1959) 173 CA2d 325, 343 P2d 341 (agreement on time of delivery)).

The merger often diminishes the seller's obligations because an ordinary grant deed is accepted without an agreement that the covenants or warranties in the purchase agreement survive closing. For covenants of title implied in a grant deed, see §§12.5-12.7. Although one solution to the merger problem is to make sure that the deed contains the necessary covenants and warranties, warranty deeds are seldom used in California. To prevent an inadvertent diminution of rights, the buyer should insist that the agreement provide that the covenants and warranties survive delivery of the deed. For a survival of warranties provision, see form 4.173-4. When the parties agree that only certain warranties will survive the closing, the provision may be drafted to include only obligations on which there is agreement. When warranties will not survive the closing, the buyer should use conditions instead and rely on investigation before the sale closes.

PRACTICE TIP: The seller will wish to limit the duration of the warranties. This can be a highly negotiated point, but a fairly common survival period for warranties on existing buildings is between 6 months and 1 year—and longer for new construction. The seller may also wish to impose a monetary limit on its liability for warranty claims. See form 4.173-4.

Deciding an issue of first impression under California law, the U.S. Court of Appeals for the Ninth Circuit concluded that a provision in a purchase agreement permitting the parties' representations and warranties to survive closing for 1 year did not also serve as a contractual statute of limitations because the provision did not unambiguously state the parties' intent to contractually reduce the applicable statute of limitations to 1 year. The survival clause merely prescribed the period of time during which a breach could occur; it did not shorten the time to file an action for breach of warranty. *Western Filter Corp. v Argan, Inc.* (9th Cir 2008) 540 F3d 947.

© The Regents of the University of California

§4.110 D. Trend Toward Limited Warranties

Modern contracts tend to have few representations and warranties by the seller. One reason for this trend is that many institutional owners of real estate, such as pension funds, take the position that giving warranties will jeopardize the assets of the investor and may be a breach of their fiduciary duty. Because many properties are owned by single-asset entities, with no recourse to the beneficial owner absent fraud, warranties are often of little benefit once the entity disburses the purchase price to its owners. As a result, many contracts are made in which the seller freely grants conditions to the buyer's obligation but limits its warranties to a warranty of authority to enter into and perform the agreement and a warranty of an absence of litigation.

© The Regents of the University of California

E. Typical Subjects for Seller's Warranties

§4.111 1. Title

The buyer might want to include both a warranty and a condition regarding title, because standard California Land Title Association (CLTA) title insurance does not cover matters that do not appear on the public record but that could be ascertained by inspecting the property or inquiring of persons in possession. A warranty is a supplement to a condition regarding title, but it is not a substitute. On CLTA title insurance policies, see California Title Insurance Practice, chaps 6-7 (2d ed Cal CEB 1997).

If the agreement includes a title warranty, the most important warranty the seller can make is that there are no off-record items that would affect title. Such a provision prevents the seller from remaining silent on any title defects of which he or she is aware. The warranty could also extend to defects of which the seller may be unaware. Moreover, defects such as encroachments are difficult to detect without surveying the property, and the buyer may not want the expense of a survey. See section 5.1.14 of Alternative 1 of form 4.173-1 for a warranty on title. On title insurance coverage generally, see Title Ins, chap 6.

The implied covenant against encumbrances under CC §1113 is not breached by visible easements that are a physical burden on the land; therefore, a warranty that there are no easements on the land other than those shown on the preliminary report should be included among those that survive delivery of the deed if the buyer does not obtain both a survey and an ALTA extended-coverage title insurance policy. If the seller intends to encumber the property with an easement, deed of trust, or otherwise, that fact should be stated. Unlike the rule on visible easements, unrecorded leases, even when known to the buyer, constitute encumbrances under §1113. *Evans v Faught* (1965) 231 CA2d 698, 42 CR 133.

PRACTICE TIP: Sellers should avoid broad representations that assets conveyed are free from encumbrances. Even a seller who does not act negligently may be liable for misrepresentation if an encroachment impairs the buyer's use of the asset. *Quality Wash Group V, Ltd. v Hallak* (1996) 50 CA4th 1687, 1694, 58 CR2d 592.

© The Regents of the University of California

§4.112 2. Physical Condition of Property

Buyers often ask sellers to warrant that the property is in good condition and repair, that no undisclosed defects exist, that the building is of a certain minimum size, and that the land contains a certain number of acres or square feet. Often the buyer's request covers all the subjects covered in the discussion in §§4.77-4.82 on the buyer's due diligence regarding the property's physical condition. The buyer seeks such warranties to force the seller to disclose defects and to guarantee the size of the property in question. Sometimes buyers request the warranties to avoid the expense and inconvenience of conducting extensive due diligence or obtaining a survey.

NOTE: Representations and warranties relating to the environmental condition of the property have become increasingly important. Very few commercial purchase agreements are silent as to the presence or absence of hazardous materials on, in, under, or around the property. See §4.80. See form 4.173-1, Alternative 1, section 5.1.16 (buyer's form) and Alternative 2, section 5.1.6 (seller's form) for purchase agreement provisions and chap 7 for a detailed discussion on hazardous waste considerations (including alternative purchase agreement provisions).

Sellers frequently respond that the buyer is responsible for conducting its own due diligence. The seller will make its books and records available to the buyer for inspection but will not warrant either the physical condition or the size of the property. Compromise positions often involve limiting the seller's warranties as discussed above. Moreover, the seller is obligated to disclose material facts about the property that would not be apparent to a buyer on an inspection, if those facts are known to the seller. See §4.49. Of course, any misrepresentation by the seller is actionable. See, *e.g., Cory v Villa Props.* (1986) 180 CA3d 592, 225 CR 628.

Care must be taken to avoid ambiguities about what is included or excluded in the area of the property. One solution is for the seller to give a warranty on the area of the property and state what is excluded in computing the area. If the purchase price is not computed using a formula based on area and if there is no representation setting out the area, the buyer who discovers after the closing that the size of the property is less than he or she believed has no cause of action against the seller. *Cory v Villa Props., supra*. Some sellers refuse to give such a warranty and insist that the buyer obtain a survey that establishes the area of the property as part of the buyer's due diligence investigation.

© The Regents of the University of California

§4.113 3. Zoning

A buyer who does not intend to change the use of the property may request a warranty by the seller that the property and all uses on it comply with existing zoning and that all necessary zoning and use permits have been obtained. The seller will wish to limit any warranty to the existing zoning classification, without broadening the warranty to describe the specific uses covered by the zoning classification. In any event, the buyer's attorney should examine the zoning law and confer with the applicable zoning department to ascertain the property's available uses, bearing in mind the possibility of future zoning changes. In addition, the buyer could obtain a zoning endorsement to its title insurance. On zoning, see §4.86. See also California Title Insurance Practice §§6.36, 7.97-7.99, 8.101 (2d ed Cal CEB 1997).

© The Regents of the University of California

§4.114 4. Subdivision Map Act Compliance

As noted in §4.92, the buyer will want to confirm that the property as it is being sold complies with the Subdivision Map Act (Govt C §§66410-66499.37). Because the seller is in a better position to know the history of the property, the buyer will want a warranty that the property complies with the Act. The seller, however, will prefer that the buyer rely on a certificate of compliance (under Govt C §66499.35(c)) or a title insurance endorsement (see California Title Insurance Practice §7.95 (2d ed Cal CEB 1997)), as described in §4.92. For a provision warranting that the property complies with the Act, see form 4.173-1, Alternative 1, section 5.1.2. If the buyer is purchasing the property to subdivide, a warranty of the property's compliance with the Map Act in its existing condition may still be appropriate. On the Map Act generally, see California Subdivision Map Act and the Development Process (2d ed Cal CEB 2001).

PRACTICE TIP: If the property is being purchased for development, the buyer will want to obtain warranties from the seller that there are no restrictions on such development except as disclosed in recorded documents (such as a development agreement), the tentative map or vesting tentative map, environmental documents (such as the environmental impact report), or other documents provided by the seller to the buyer during its due diligence. See form 4.173-1, Alternative 1, section 5.1.12.

© The Regents of the University of California

§4.115 5. Violation of Other Governmental Requirements

The buyer often seeks warranties protecting against violations of law that affect the property or its use. One kind of protection is a warranty that no violations exist. There can be many variables in negotiating this provision. For example, a provision favorable to the buyer might require the seller to cure all violations or indemnify the buyer against claims, liabilities, damages, legal fees, and expenses incurred by the buyer because of violations. In response, the seller may wish to, *e.g.:*

- Condition the seller's obligation on notification by the buyer within a limited time after discovery of the violation;
- Limit the seller's obligation to violations officially noted in governmental records;
- Limit the warranty to violations in existence at the time of execution, rather than at closing, to prevent the buyer from bringing an enforcement action as a defense to the contract;
- Allow the seller to have the violation dismissed of record rather than curing it;
- Limit the warranty to violations known to the seller;
- Require the buyer to share the expense of curing violations; or
- Limit the cost of curing violations to a fixed amount or to the damage that would otherwise result.

An alternative is a warranty that the seller has no knowledge of (or that seller has not received a notice of) a violation or an order of an applicable governmental authority requiring performance of any repair or improvement, a notice of condemnation, or a notice from a governmental agency or a board of fire underwriters that the property does not comply with current codes or building standards.

In addition to the seller's warranty on the state of the property on the sale date, the buyer will want to know whether any governmental agency is taking any action that would affect the property in the future, including any pending or threatened condemnation or assessment. See form 4.173-1, Alternative 1, section 5.1.9. The seller is in the best position to know of such actions because the property owner must be notified at some stage of the proceeding. The seller will not want to give a warranty as broad as that, because the seller either may not know of such matters or, if the seller did receive notice of a proceeding, may have forgotten or misplaced it. One way to reduce the scope of the warranty is to limit it to the seller's actual knowledge. See form 4.173-1, Alternative 2, section 5.1.8.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.116 6. Litigation

§4.116 6. Litigation

The buyer must know whether litigation affecting the property is pending. Such litigation may include, *e.g.:*

- Mechanics' lien foreclosure actions;
- Unlawful detainer actions (if the seller is transferring a tenant's interest in a ground lease, such an action could eliminate the estate being transferred); and
- Actions by governmental agencies for violations on the premises.

The preliminary report should show if a notice of pending action (lis pendens) involving litigation affecting the property has been recorded and properly indexed. Under former CCP §409.9, anyone who entered into a contract to transfer an interest in real property and who received a notice of lis pendens concerning the property was required to notify prospective transferees of that notice within 3 days. That requirement was not incorporated into the replacement legislation (CCP §§405.20-405.24). To avoid claims of misrepresentation or concealment by prospective transferees under a contract, it would still be prudent, however, for the transferor of any interest in the property to notify transferees of its receipt of a notice of pendency of action. See California Real Property Remedies and Damages §13.16 (2d ed Cal CEB 2002). Moreover, because the buyer's knowledge of such actions is crucial and the information may not otherwise be easily discoverable, most agreements contain a warranty by the seller regarding litigation. The warranty may be limited to the seller's knowledge, but it often includes the threat of litigation in addition to pending litigation. See form 4.173-1, Alternative 1, section 5.1.6.

© The Regents of the University of California

§4.117 7. Books, Records, Leases, and Contracts

The buyer will ask the seller to confirm that all material books, records, leases, contracts, and reports on the property have been delivered to the buyer. For buyer's form, see form 4.173-1, Alternative 1, section 5.1.3. For seller's form, see form 4.173-1, Alternative 2, section 5.1.1.

In particular, the buyer needs to know whether he or she will acquire any contractual obligations by purchasing the property. Many buyers will request a warranty that no undisclosed agreements exist or, if they do, that the seller must compensate the buyer for any liability incurred under them. Some buyers request an assurance from the seller that all documentation delivered to the buyer is accurate; many sellers resist giving such a warranty and state only that accurate copies were delivered.

The buyer also wants to know whether the seller is in default under any leases or other agreements, such as easements, declarations of covenants, conditions, and restrictions, deeds of trust, management or maintenance contracts, or agreements relating to the development of the property or to provide utilities. The seller's default under a lease may entitle the tenant to terminate the lease or withhold rent. A default by the seller under a deed of trust may entitle the lender to accelerate the loan. A requirement that the document be inspected might be enough to satisfy and protect the buyer, but in other cases the buyer may request an estoppel certificate from the other party to the agreement.

© The Regents of the University of California

§4.118 8. Authority

If the seller is an entity, it will customarily represent that it was duly formed and is duly authorized to enter into and perform the agreement. For buyer's form, see form 4.173-1, Alternative 1, section 5.1.13. For seller's form, see form 4.173-1, Alternative 2, section 5.1.1.

© The Regents of the University of California

§4.119 F. Typical Buyer's Warranties

Only a few warranties are appropriate for a buyer. If the buyer is an entity, for example, it would be appropriate to warrant that it has been duly organized and is duly authorized to enter into and perform the agreement. See section 5.2.1 in form 4.173-2. Some sellers insist on a warranty that the buyer is financially able to perform under the agreement, and many sellers request that the buyer represent that it is not involved in any litigation affecting the property or the transaction.

Since the enactment of the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (USA Patriot Act) (Pub Law 107-56, 115 Stat 272), buyers are often required to provide "anti-terrorism" representations and warranties. Executive Order 13224 prohibits, among other things, transactions in real property with any person identified as a "Specially Designated National" or blocked person. A list of Specially Designated Nationals is published by the Department of the Treasury, Office of Foreign Assets Control (OFAC) and can be found on their website. See Directory for site. Violation of the order carries both civil and criminal penalties, including civil penalties of up to $1 million per violation, as well as jail terms of up to 10 years for individual violators. 31 CFR §501.701.

Sellers should exercise diligence in determining that the buyer is not a Specially Designated National or blocked person. It is advisable to include a representation and warranty to such effect in the purchase agreement. A seller should not rely, however, on the representation alone. A seller (or seller's counsel) should compare the purchaser's identification with the OFAC's list. In the event of a possible match, the seller should evaluate the quality of the match and contact the OFAC's Compliance Programs Division at 1-800-540-6322. From the buyer's perspective, the buyer will want the representation to be narrow in scope, *i.e.*, based on an "actual knowledge" standard or applicable only to itself or, if an entity, to those persons controlling the entity such as members, partners, or shareholders of a privately held corporation. See sample provision in section 5.2 of form 4.173-2.

© The Regents of the University of California

§4.120 G. "As Is" Provisions

If the seller does not want to make warranties on the condition of the property and if market conditions allow that advantage, an "as is" provision, which puts the entire burden of ascertaining the condition of the property on the buyer, may be used. See form 4.173-5. An "as is" provision does not excuse a seller from disclosing hidden material defects known to the seller. Failure to disclose such matters constitutes fraud, and the "as is" provision applies only to visible, observable matters. *Lingsch v Savage* (1963) 213 CA2d 729, 29 CR 201. See also *Katz v Department of Real Estate* (1979) 96 CA3d 895, 158 CR 766. Furthermore, an "as is" provision does not exempt a seller from other disclosure requirements imposed by statute, such as CC §§1102-1102.17 and Health & S C §25359.7. Any waiver of the requirements of CC §§1102-1102.17 is void as against public policy. CC §1102(c). This law supersedes language in *Loughrin v Superior Court* (1993) 15 CA4th 1188, 19 CR2d 161, that the Transfer Disclosure Statement for one-to-four-unit residential property can be waived if the waiver is done knowingly and explicitly. See §6.8.

© The Regents of the University of California

IX. CLOSING CONDITIONS

§4.121 A. Purpose of Closing Conditions

There are two sets of conditions in typical purchase agreements: First are the buyer's due diligence conditions; once those conditions are satisfied, the buyer risks losing its deposit and being subject to the seller's other remedies if the buyer defaults. Second, after the buyer's due diligence conditions have been met, agreements customarily include conditions to the obligations of both buyer and seller to close under the agreement.

© The Regents of the University of California

B. Typical Buyer's Conditions

§4.122 1. Title Insurance

Although the buyer will have approved the state of title during its due diligence investigation (see §§4.50-4.69), its obligation to purchase the property should be subject to an express condition that it obtain title insurance as of closing in the form approved. There is no implied obligation of the seller to provide or pay for title insurance and no implied condition to the buyer's obligation to purchase the property that title insurance be issued. *Easton v Montgomery* (1891) 90 C 307, 27 P 280; *Seymour v Shaeffer* (1947) 82 CA2d 823, 187 P2d 95, disapproved on other grounds in *Ellis v Mihelis* (1963) 60 C2d 206, 216, 32 CR 415. The agreement should expressly provide for it. See section 6.1.1 of form 4.174-1. Payment of the title insurance premiums, however, is a matter of negotiation between the parties; see §4.134.

On the available forms of title insurance, see California Title Insurance Practice, chaps 6-7 (2d ed Cal CEB 1997). The amount of coverage is customarily equivalent to the purchase price, although this may vary. On endorsements, see Title Ins §§7.64-7.103A (owner's endorsements), 8.50-8.118 (lender's endorsements). On selection of a title insurance company, see §4.53.

If the buyer believes that personal property may be encumbered, it should require a UCC search as part of the escrow to discover what encumbrances exist and require the escrow holder to pay the encumbrances at closing. See §4.33. On UCC filings generally, see Secured Transactions in California Commercial Law Practice, chap 3 (2d ed Cal CEB 2001).

If the majority of the seller's assets are being sold, the bulk sales requirements of Com C §§6101-6111 may have to be satisfied.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.123 2. Other Conditions

§4.123 2. Other Conditions

Other typical conditions for the buyer include the following:

- Seller will deliver the documents as required by the agreement (see section 6.1.6 of form 4.174-1);
- Seller's representations and warranties will be true at closing (confirmed by delivery of a certificate) (see section 6.1.3 of form 4.174-1); and
- Seller will perform other obligations (such as delivery of estoppel certificates or completion of construction) at or before closing (see section 6.1.4 of form 4.174-1).

For form of buyer's closing conditions generally, see section 6.1 of form 4.174-1.

© The Regents of the University of California

§4.124 C. Typical Seller's Conditions

Typical seller's conditions are the following:

- Buyer will deliver the purchase price (see section 6.2.2 of form 4.174-2) and any prorated amounts due from buyer (see §4.133);
- Buyer will deliver all required documents (see section 6.2.3 of form 4.174-2); and
- Buyer's representations and warranties will be true at closing (see section 6.2.4 of form 4.174-2).

For form of seller's closing conditions generally, see section 6.2 of form 4.174-2.

© The Regents of the University of California

§4.125 D. Releases and Waivers by Buyer

Some sellers request that the buyer waive all claims regarding the property and release all claims against the seller. Such provisions are always highly negotiated. These waivers usually exclude warranties that survive closing, covenants in the grant deed, other obligations of the seller that the parties agree should survive closing (such as indemnity obligations), and claims based on fraud or misrepresentation.

Waivers and releases of claims based on the presence of hazardous substances on the property are often included in the agreement. Sellers take the position that all facts regarding the property that were disclosed to or found by the buyer are reflected in the purchase price, including the presence of any hazardous substances.

The seller remains liable for failure to disclose material facts known to it, and the buyer takes the risk of unknown and undiscovered matters. See form 4.173-6.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.126 E. Closing Subject to Another Transaction

§4.126 E. Closing Subject to Another Transaction

For various reasons, one party may not wish to complete the transaction without some other transaction occurring. The contractual solution in virtually all cases is to condition the other party's performance on the occurrence of the other transaction. The protection for the opposing party is to place time limits on various steps in the completion of the other transaction and to be given evidence of completion of those steps. A carefully negotiated agreement would provide the following:

- The party in whose favor the condition runs must enter into the contract for the other transaction by a given date —otherwise, either party may terminate the agreement;
- The party in whose favor the condition runs must complete due diligence in the other transaction by a given date, with mutual termination rights for failure; and
- The other transaction must close either simultaneously with the subject transaction or before it is scheduled to close.

Opposing parties sometimes request that the party imposing the condition also agree to enter into and perform the other transaction, which would give a right of damages if breached. Most parties resist this requirement.

Examples of transactions subject to the closing of another transaction are described in §§4.126-4.131.

© The Regents of the University of California

§4.127 1. Simultaneous Exchange

The most common factual circumstance in which closing is subject to another transaction occurs when a seller wishes to engage in a simultaneous three-way exchange under IRC §1031. The seller wishes to defer gain on disposition of its property by exchanging it for another property that it wishes to acquire. Two-party exchanges, in which the seller and the buyer exchange properties they own, are extremely rare. More often, the seller locates the property it wishes to acquire (the "target property") and then structures the transaction as a three-way exchange. The theory is that the buyer buys the target property and exchanges it for the property being disposed of by the seller. In fact, parties conduct the three-way exchange in a single escrow: The buyer places its purchase price in escrow, the seller provides a deed to the buyer for the seller's property, and the owner of the target property provides a deed to the seller for the target property and receives the cash consideration. Subject to adjustment for receipt or payment of cash by the seller or relief of mortgage indebtedness by the seller, the seller's recognition of gain for federal and state income tax purposes is deferred until the target property (or its replacement property) is sold. After the transaction, the cost basis of the target property will be the cost basis of the property disposed of by the seller.

The risk for the buyer is that the purchase of the target property may not close. In addition, sellers often have not selected a target property before the sale of the seller's property to the buyer is ready to close. For these reasons, sellers more often engage in delayed or deferred exchanges (discussed in §4.165). See generally IRC §1031; Treas Reg §1.1031(k)-1; Real Property Exchanges (3d ed Cal CEB 2002).

To protect itself in a simultaneous exchange, the buyer should require the seller to identify the target property within a given time, enter into an agreement to acquire the target property or exchange it by a given date, complete due diligence by a given date, and agree to close that transaction at the same time as the primary transaction. The buyer will also insist that the seller indemnify the buyer for any costs or expenses in connection with the exchange. The buyer will attempt to insist that its acquisition of the seller's property proceed whether or not the exchange occurs, but the seller will usually reject such a requirement because it would incur tax, which the seller is attempting to avoid. For the same reason, a seller would permit the agreement to include conditions in favor of the buyer as discussed in §§4.122-4.123, but it would not include covenants that would give the buyer a remedy for damages or specific performance.

For an accommodation provision for a tax-deferred exchange, see form 4.178-15.

© The Regents of the University of California

§4.128 2. Multiple Sellers

If the property being sold is owned by multiple owners with undivided interests, whether tenants in common or joint tenants, the best approach for the buyer is to enter into a single agreement with all owners. Often, the owners' signatures should be obtained with counterpart signatures. For a counterpart signature provision, see form 4.178-14.

When it is not possible for the buyer to enter into a single agreement with all owners of undivided interests, the buyer must enter into several agreements, all conditioned on each other. Each seller may want various deadlines to be met for waiver of due diligence conditions and closing, and all deadlines should be coordinated. The buyer should insist that if it terminates one agreement, for whatever reason, it may terminate all the agreements, and if any seller terminates one agreement, the buyer may terminate all other agreements. A seller may object to such interdependence of multiple agreements. A buyer would note that the better solution, a single agreement, cannot be achieved, owing to the lack of cooperation among the sellers. As a result, in most situations the sale can proceed on no basis other than interdependent conditions among the several agreements. Each seller will want the right to terminate its agreement if conditions are not met by a set date.

© The Regents of the University of California

§4.129 3. Removal of Title Defect

If a title defect exists that must be removed as a condition of closing, often the party removing the condition must enter into an agreement with the holder of the right in question in order to correct the defect. Examples of removing such defects include the following:

- Purchasing an easement encumbering the property;
- Terminating a right of surface entry held by the owner of the mineral rights under the property; or
- Acquiring an undivided interest held by an uncooperative owner.

Sometimes the seller must remove the defect in order to entice the buyer to purchase the property at the negotiated price. In strong sellers' markets, the buyer might take responsibility for removing the defect. Either way, the party removing the defect must enter into an agreement with a third party and agree to pay the necessary consideration.

All the issues of timing discussed in §4.126 apply to this situation. In some cases, a buyer may not agree to start its due diligence until the seller has entered into an agreement to remove the defect (which itself would be subject to the condition that the buyer close the transaction to purchase the property). Negotiation of such ancillary transactions are often time-consuming and should be provided for in drafting the purchase agreement. Buyer's counsel may (1) make buyer's obligations under the purchase agreement contingent on the seller's entering into an agreement to remove the defect (section 3.4.3 in form 4.171-4), or (2) make buyer's obligation to close conditioned on seller's removal of the defect at or before closing, or both (section 6.1 in form 4.174-1).

© The Regents of the University of California

§4.130 4. Purchase of Additional Property

A buyer's purpose in purchasing the subject property can often be fully realized only by acquiring additional property. Examples include adjoining property that is necessary to complete the assembly of the parcels required by the buyer or an easement needed for access. Depending on the circumstances, the additional property, easement, or other interest can be acquired by either the buyer or the seller. In any event, the condition in the purchase agreement must state the date when an agreement will be entered into with respect to the other property, when due diligence will be completed on the other property, and when the other transaction will close. Often, a buyer will insist that its due diligence period under the main agreement not expire until an agreement is entered into with respect to the other property and due diligence has been completed. The buyer will also want the right to approve due diligence matters on the other property.

Closing under both agreements is often simultaneous. The seller will insist that a strict timetable be followed, with a cancellation right if it is not. If the seller is to acquire the other parcel or interest, the considerations are similar.

© The Regents of the University of California

§4.131 5. Sale of Another Property by Buyer

Frequently, the buyer must sell a property it owns in order to purchase the property in question. This situation occurs most often in residential transactions, but it can also occur in commercial transactions. A likely circumstance in a commercial transaction is the acquisition of property by a user to house its business. In a strong sellers' market, a seller will refuse to permit a condition to the agreement that a third property be sold by the buyer. In other markets, the seller will permit such a condition, but require that a contract for the sale of the other property be entered into by a set date, that due diligence conditions be waived by the buyer of the other property by a set date, and that the closing of both transactions also occur by a date set in the agreement.

© The Regents of the University of California

X. ESCROW AND CLOSING

§4.132 A. Closing Through Escrow

Virtually all California real estate transactions close through an escrow. Purchase agreements often serve as joint escrow instructions to the escrow holder, although in complex commercial transactions supplemental escrow instructions (often executed jointly between buyer and seller) are usually required. A lender will also require its own form of supplemental escrow instructions relating to the disposition of the loan proceeds and recordation of its security documents. Escrows and closing are discussed in chap 15.

The purchase agreement should state the intended closing date, the last date to close, the documents and funds that will be exchanged at closing through escrow, and the other actions to be taken at closing. For form of escrow instructions within the purchase agreement, see forms 4.175-3 through 4.175-10 under Article 7, which lists the documents and funds to be provided by the buyer and the seller.

The seller must provide the following:

- The deed;
- An assignment of any leases and service contracts to be assigned;
- A bill of sale for any personal property; and
- Certification under the Foreign Investment in Real Property Tax Act of 1980 (FIRPTA) (see IRC §§897, 1445; Rev & T C §18662). For form certification, see App T.

NOTE: Effective January 1, 2007, an alternative calculation exists to determine any required withholding taxes on the purchase price. See Rev & T C §18662. For a detailed discussion, see §§15.75-15.80.

Original copies of leases, a rent roll, documents on the property, and keys to the property are typically delivered outside of escrow.

The buyer must provide the following:

- Funds necessary to close; and
- An agreement assuming any leases and any financing documents.

A timely close of escrow is usually crucial to both parties. Most escrow holders record their documents at the commencement of a business day after checking them over the day before. Some counties do not permit escrow holders to record documents after the commencement of a business day unless special arrangements are made. It is seldom possible to complete the necessary recording on the date scheduled for the close of escrow if all papers and funds are not in the hands of the escrow holder by the business day before the scheduled date to close escrow. See chap 15 on escrows and closing.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.133 B. Prorations

§4.133 B. Prorations

The agreement should provide for the proration of income and expense items relating to the property. See form 4.175-7. Taxes, rents, insurance, and all other costs or income items transferred from the seller to the buyer are traditionally computed on a daily basis and divided between the buyer and the seller as of the closing date. The adjustments are usually made in cash through the escrow. The amount of the rent and deposits is set out in the seller's rent statement, which should be subject to the buyer's approval. The buyer can confirm the accuracy of the rent statement from the tenants' estoppel certificates. The seller should be required to warrant the accuracy of the rent statement to the extent it is not feasible to obtain estoppel certificates. See also §§4.73, 4.101.

If rent for the month in which the closing occurs has not been paid, the parties must state in the agreement how that issue will be resolved. Typically, the buyer does not want to inherit the arrearages, and the seller fears that, without the leverage of being the landlord, the sum may never be collected. The usual compromise is that the seller retains the right to collect rent payable before closing from the tenant and the buyer agrees to cooperate with the seller to collect it. If the amount of percentage rent or cost pass-throughs that a tenant pays cannot be calculated at the closing, a provision for a post-closing proration must be added.

If there is no current tax bill and the previous year's bill does not afford a reasonable basis for estimating the current year's bill, the parties may agree on a specified daily amount pending receipt of the future tax bill. This problem arises when the closing occurs between July 1 and the time the tax bill for the current year becomes available, usually sometime in October. See Rev & T C §2610.5. Alternatively, the agreement could provide that a specified sum will be adjusted outside of escrow when the bill is received. This procedure, however, complicates the transaction by requiring that a calculation be made after the closing. To simplify computations, a 30-day month is often specified as the basis for prorations.

The county assessor may make a retroactive change in the assessed valuation if there was new construction or a change in ownership before the sale that is not reflected in the tax roll by the time of the sale. A supplemental tax bill will be issued when the reassessment is made. The prorations provision (and the escrow instructions; see §§15.44, 15.68) should provide for the proper proration of any supplemental tax bill issued before the close of escrow. See section 7.7.5 of form 4.175-7. Any prorations based on a supplemental tax bill issued after the close of escrow will have to be handled between the buyer and the seller by an agreement outside of escrow. On liability for payment of taxes based on escape assessments, see Rev & T C §531.2.

Insurance premiums are prorated only if the seller's insurance can be transferred and if the buyer and the seller desire to transfer it.

Other items that may be prorated are the following:

- Installment payments on personal property being transferred with the real property;
- Homeowner's association assessments in common interest developments; and
- Interest on loans assumed by the buyer.

If a loan being assumed has an impound account, the account should be assigned to the buyer and the seller should be credited with the balance. Interest is not prorated on an underlying note when an all-inclusive note or wraparound deed of trust is used.

Treatment of assessments for improvements encumbering the property must be negotiated. See §4.63. The agreement should specify whether the seller is to pay off the assessment before close of escrow, or the buyer is to take title subject to the assessment but with a credit against the purchase price, or the buyer is to take title subject to the assessment without any credit against the purchase price. Interest on the assessment should be prorated to the closing date if it is assumed by the buyer.

When the real property being sold is part of a parcel under one assessment, the periods before and after closing present separate problems. For the period before closing, because segregation of taxes is not possible before ownership is transferred, the division must be made by agreement to prorate based on an allocation of value between

the property sold and the remaining part of the seller's land. For discussion and provisions, see §§15.43, 15.57, 15.68. For the period after closing, all taxes should be separately assessed to each parcel resulting from the sale. Segregation is authorized by Rev & T C §2821. The application and affidavit of interest must be made during the current fiscal year. A county may prohibit applications during the 10-day period preceding each tax installment delinquent date (December 10 and April 10) and during the 10-day period before June 30 of each year.

© The Regents of the University of California

§4.134 C. Closing Costs

The division of closing costs is negotiable and can be made on any terms to which the parties agree. Once the division is decided, it should be clearly stated to avoid disputes. Almost without exception, the seller pays for all costs of clearing title and delivering the grant deed; the buyer pays for all costs in connection with any new financing. The parties typically follow the custom in each county. The seller often pays the county documentary transfer tax, but customs differ with respect to payment of city or other local transfer taxes, which are often split between the buyer and the seller. The issuance, transfer, or exchange of a security or the making or delivery of an instrument of transfer pursuant to a plan confirmed under Chapter 11 of the Bankruptcy Code is exempt from state or local transfer taxes. 11 USC §1146(a). The transfer tax exemption applies only to transfers made pursuant to a confirmed Chapter 11 plan. *Florida Dep't of Revenue v Piccadilly Cafeterias, Inc.* (2008) ___ US ___, 171 L Ed 2d 203, 128 S Ct 2326. In Bay Area counties, the buyer generally pays both the escrow fee and the title insurance premium; in Southern California, the seller usually pays the title insurance premium, and the escrow fees are divided. Elsewhere, both charges may be divided. See §15.42 on closing costs; and see form 4.175-8.

Other costs that might be specified in this provision are the following:

- The additional cost of an extended-coverage American Land Title Association policy of title insurance above California Land Title Association coverage;
- The cost of any special title policy endorsements;
- The cost of any survey that might be required; and
- Any prepayment penalty charged by a lender.

PRACTICE TIP: Buyer's counsel should investigate the amount of a city's transfer tax before agreeing to split the cost with the seller, because many cities impose a transfer tax significantly higher than the county tax. For example, Oakland's transfer tax is equal to 1.5 percent of the "value of consideration" paid for the property (generally the purchase price). Thus, Oakland's city transfer tax on the sale of a $30 million commercial building is $450,000. Oakland Muni C §4.20.020.

© The Regents of the University of California

§4.135 D. Brokerage Fees

Both parties will wish to avoid claims for commissions or finder's fees after the closing. The agreement should state the commissions to be paid and provide that each party will indemnify the other against any claims that any other fee or commission is due because of that party's acts. See form 4.175-9.

The broker's commission is determined by the broker's written agreement with the client. See §2.94. Usually, this issue is covered in the listing agreement. If none was executed, the broker must rely, as a third party beneficiary, on the purchase and sale agreement or escrow instructions to supply the writing required by CC §1624(a)(4). See §2.54. To avoid difficulties, the drafter should ascertain who is to receive what commission or fee, who is to pay, and when the commission is considered earned. Then all parties, including the broker, should confirm in writing that the amount is correct. Without the broker's written acknowledgment, confusion will arise over whether the controlling document is the original commission agreement signed by the broker or the later purchase and sale agreement. If this provision is included in the sale agreement, each broker should sign the agreement on the signature page. Many purchase agreements provide that the commission will be paid according to the listing agreement. Payment of the commission should be conditioned on closing the transaction; thus, no commission is due if the sale is not completed.

If a licensed real estate broker or salesperson acting as an agent in the transaction is also a party to the agreement, or holds a direct or indirect interest in one of the parties, the licensee must disclose that fact. Bus & P C §§10176(i), 10177(o). It is immaterial that the transaction is otherwise fair to the parties. *Batson v Strehlow* (1968) 68 C2d 662, 68 CR 589; *Smith v Zak* (1971) 20 CA3d 785, 98 CR 242.

© The Regents of the University of California

§4.136 E. Possession

As a rule, the seller agrees to deliver possession of the property to the buyer at closing. See form 4.175-10. If the seller wishes to remain in possession after the closing date, the parties should agree to a daily rental rate. A sum sufficient to pay the anticipated rent, plus a security deposit, should be delivered to the buyer through escrow at closing pending the seller's delivery of possession. Civil Code §1950.5 limits the amount of the security deposit for residential property. A security deposit protects the buyer if the seller holds over or damages the property or if the buyer must bring an unlawful detainer action to obtain possession. An unlawful detainer action can be initiated, without prior service of notice, against a tenant who holds over after a fixed rental term has expired. CCP §1161(1). The agreement should provide that the seller is a tenant at sufferance after the tenancy term expires, that the provision on holding over survives closing, and that the seller will indemnify the buyer from any losses if the seller fails to vacate the premises on time.

PRACTICE TIP: A "hold-over" provision in the agreement should be used only if the seller will remain in possession for a short period of time and if there are no complicated landlord-tenant issues. As a rule, it is preferable to address a seller's hold-over possession by having the seller sign a lease or rental agreement that will become effective on the closing and will set forth all terms and conditions of the seller's occupancy of the property.

© The Regents of the University of California

§4.137 XI. RISK OF LOSS

Unless the agreement provides otherwise, the Uniform Vendor and Purchaser Risk Act (CC §1662) governs the risk of a casualty loss to the property or acquisition of all or a portion of the property by eminent domain after the purchase and sale agreement is executed. This Act provides generally that, if all or a material part of the property is destroyed or condemned, the seller cannot enforce the contract and the buyer is entitled to recover any portion of the price paid if neither legal title nor possession was transferred.

NOTE: To avoid the uncertainties and expense of litigation over what constitutes a "material loss," a purchase and sale agreement that apportions risk based on the Act should include a definition. See form 13.5-1.

If the casualty or the portion of the property taken by eminent domain is not "material" (see §§13.4-13.5), the implication of the statute is that the buyer bears the risk of loss but the purchase price is not reduced by the amount of the loss. If either legal title or possession was transferred, all loss falls on the buyer. CC §1662(b). See chap 13 on risk of loss and property insurance, particularly §§13.3-13.14.

In the authors' experience, the provisions of the Act rarely reflect the intentions of parties to agreements. Parties often wish to treat condemnation separately from casualty losses and draft provisions on casualty losses tailored to the property that is the subject of the contract. See form in §4.176. In such cases, however, the parties should specify in the contract the extent to which they intend the Act to apply, because the inclusion of any provision relating to risk of loss may make the entire Uniform Vendor and Purchaser Risk Act inapplicable on the grounds that the parties have "provided otherwise." *World Exhibit Corp. v City Bank Farmers Trust Co.* (App Div 1946) 61 NYS2d 889, aff'd (1946) 296 NY 586, 68 NE2d 876 (construing statute similar to CC §1662). To meet this problem, it is desirable to state that the Act will apply to the extent it does not conflict with the contract. See §§13.3-13.10.

© The Regents of the University of California

§4.138 A. Condemnation Loss

Many agreements include a provision on condemnation that is separate from the provision on casualty losses. See form 4.176-1. Many buyers insist that they have the option to withdraw from the agreement in a condemnation, which leaves the buyer free to choose its course of action. Sellers will attempt to limit the buyer's discretion. The items for negotiation include the portion of any building taken by eminent domain, the portion of the land (excluding buildings) taken, loss of access, and loss of parking. Other matters may be relevant to a particular property. Often, a simple street widening will not harm the buyer's interests, but nevertheless the buyer will often wish to review and approve the actual condemnation, rather than giving a general consent when the agreement is negotiated.

PRACTICE TIP: The parties may often find that negotiation of a condemnation provision tailored to the specific circumstances will serve their interests better than the Uniform Vendor and Purchaser Risk Act (CC §1662).

© The Regents of the University of California

§4.139 B. Casualty Loss

In many transactions, casualty provisions should be specifically negotiated. At the least, the parties should agree on the definition of "material" in terms of the dollar cost of reconstruction. See form 13.5-1. More often, contracts require the seller to maintain casualty insurance and, in a casualty deemed "immaterial" by the agreement, provide that the transaction will proceed, and insurance proceeds under the required insurance and any deductible amount will be paid by the seller to the buyer at closing. In the event of casualty losses with a reconstruction cost larger than the amount specified as "material," the buyer has the option to receive the insurance proceeds and then close or cancel the transaction. In general, it is better to give the buyer the choice in the event of a casualty defined as material, rather than require that the transaction be terminated.

In some transactions, the seller has no insurance (or is self-insured) and demands that all risk of loss be transferred to the buyer when the purchase agreement is executed. At that time, the buyer has an insurable interest and can obtain the insurance it chooses. See §13.11. Most buyers will object to such a provision, however, because possession is usually not transferred until closing and the buyer will not control the use or occupancy of the property until after closing. See discussion in §§13.11-13.12.

It bears repeating that the insurance provisions of the agreement must be coordinated with the casualty provisions. If the seller is at risk after the contract is signed and before closing, it is in the seller's interest to carry appropriate casualty insurance and it is in the buyer's interest to require the seller to do so. If the seller is self-insured or carries a large deductible, the buyer must analyze the credit risks involved and consider modifications to the purchase agreement or establish requirements for seller's insurance that protects the buyer's interests. For a casualty loss form, see form 4.176-2.

© The Regents of the University of California

XII. DEFAULT AND REMEDIES

§4.140 A. In General

The parties to a real property purchase and sale agreement have a variety of statutory remedies available if the other party breaches the agreement. No contract provisions need be added to secure these remedies, which include the following:

- Damages for breach of contract under CC §3300;
- Buyer's damages under CC §3306, if the seller fails to convey;
- Seller's damages under CC §3307, if the buyer fails to buy;
- Tort damages for fraud and misrepresentation; and
- Equitable remedies of specific performance, rescission, and reformation.

See generally California Real Property Remedies and Damages (2d ed Cal CEB 2002). The drafting issues regarding remedies concern changes the parties wish to make to the remedies that are available in the absence of other provisions. The most common changes are the addition of provisions liquidating the seller's damages in the event of the buyer's breach (see form 4.177-2) and limiting the buyer's remedies for the seller's breach. See form 4.177-4. Also, the parties should add provisions requiring notice to the other party before a default may be declared. See forms 4.177-1, 4.177-3.

© The Regents of the University of California

B. Seller's Remedies

§4.141 1. Damages

The seller's damages for the buyer's failure to purchase the property are prescribed in CC §3307. The seller can recover the loss of its bargain (*i.e.,* the difference between the purchase price stated in the agreement and the "value of the property to him or her"), consequential damages, and interest. The seller can also recover its special damages for such expenses as brokerage commissions and resale expenses. See California Real Property Remedies and Damages §§4.30-4.38 (2d ed Cal CEB 2002).

In practice, the seller's damages may be limited. It cannot recover its "loss of bargain" damages if the property is worth more than the sale price when the buyer breaches, or if the value exceeds the sales price at or before the time of the trial. See *Spurgeon v Drumheller* (1985) 174 CA3d 659, 220 CR 195. Nor can the seller recover consequential damages from a defaulting buyer after a sale to another buyer at a higher price; such damages would be contrary to CC §3358, which provides that one cannot recover more as damages for breach "than he could have gained by the full performance thereof on both sides." *Smith v Mady* (1983) 146 CA3d 129, 133, 194 CR 42. In light of such decisions, sellers often insist on including a liquidated damages provision (see §4.142) in the agreement, particularly in a rising market. Such a provision also reassures the buyer that there is a limit to its exposure.

© The Regents of the University of California

§4.142 2. Liquidated Damages

Virtually all California real estate purchase agreements contain a provision liquidating the seller's damages for the buyer's breach. The liquidated damages usually equal the amount of the buyer's deposit. Under CC §§1671, 1675-1681, a liquidated damages provision is usually valid unless the party seeking to invalidate it establishes that it was unreasonable under the circumstances existing when the contract was made. CC §1671(b). See generally Guggenhime, *California's New Liquidated Damages Law*, 1 CEB Real Prop L Rep 17 (Feb. 1978). The statutes do not limit either party's right to seek specific performance, nor do they affect installment land sale contracts under CC §2985. A provision liquidating the seller's damages is in form 4.177-2.

In real property transactions, a provision liquidating damages to the seller for the buyer's breach is subject to the additional requirements that it must be separately signed or initialed by each party to the contract (CC §1677(a)), and, if printed, must be set out in at least 10-point bold type or in contrasting red print in at least 8-point bold type (CC §1677(b)). Liquidated damages provisions in typed agreements should be in capital letters.

In a contract to purchase one-to-four-unit residential property to be occupied by the buyer, CC §1675 imposes additional requirements regarding the deposit:

- Liquidated damages may not exceed the amount actually paid as a deposit;
- If the deposit amount is 3 percent of the purchase price or less, the provision is valid unless the buyer establishes that the amount is unreasonable;
- If the amount exceeds 3 percent of the purchase price, the provision is invalid unless the party seeking to uphold it establishes that the amount is reasonable; and
- "Reasonableness" depends on
- the circumstances at the time the contract was made; and
- the price, other terms, and circumstances in any sale or contract to sell the property made within 6 months after the buyer's default.

For special rules regarding liquidated damages on the sale of a newly constructed attached residential condominium in a project of ten units or more, see §6.45.

If the sum that is to be liquidated damages is increased, *e.g.,* through an additional payment increasing the "buyer's deposit," then a new liquidated damages provision must be signed or initialed with each increase in the deposit. CC §1678.

As a practical matter, the seller will have difficulty enforcing liquidated damages provisions without litigation if the buyer resists, because escrow holders usually require both parties' consent in writing after the breach before they will release the buyer's funds to the seller. Failing such agreement, the escrow holder may interplead the funds into court. The seller would be in a stronger position if the earnest money deposit were paid directly to the seller outside of escrow. The seller would then have the deposit in hand, and the buyer would have to sue to recover any amount claimed to be in excess of the sums allowed by law. For this reason, buyers usually resist requests to release funds from escrow.

Sellers often exclude from the protection of the liquidated damages provision the buyer's obligations under the prevailing-party attorney fees provision and any indemnification in the agreement, such as indemnities against (1) damage or injury arising from the buyer's inspection of the property, and (2) broker's commissions and finder's fees arising from the buyer's conduct.

PRACTICE TIP: Buyers should confirm that the provision states that liquidated damages will be the seller's sole remedy (except for the exclusions noted above). If the provision states only that the amount of damages the seller can recover is liquidated damages, the seller arguably retains a right to equitable remedies, including specific performance.

© The Regents of the University of California

§4.143 3. Specific Performance

Specific performance is available as a remedy for the buyer's breach if it is not waived in a liquidated damages provision and if the conditions to its availability are met. A seller might wish to preserve the remedy rather than waive it in the customary form of a liquidated damages provision. There are several practical difficulties and legal uncertainties, however, in obtaining specific performance. In the authors' experience, most sellers waive specific performance and agree that liquidated damages will be their sole remedy.

If not waived, specific performance is available only if the following conditions are met (CC §§3384-3395):

- The seller must not have an adequate remedy in the form of money damages;
- The consideration to the buyer must be adequate;
- The contract must be just and reasonable with terms that are sufficiently certain to enforce;
- The buyer must not be subject to undue hardship;
- The ordered performance must be substantially similar to that required by the contract;
- The ordered performance must not be of a type that would be impracticable for the court to supervise; and
- The seller must have performed or tendered performance under the contract and be ready to perform after the judgment.

Two of the requirements in particular cause difficult issues for sellers. The first is whether CC §3307 provides the seller with an adequate remedy for damages, despite the presumption stated in CC §3387 that breach of an agreement to transfer real property cannot be adequately compensated by money damages. In *BD Inns v Pooley* (1990) 218 CA3d 289, 296, 266 CR 815, the court held that CC §3307 was not intended to eliminate the seller's right to seek specific performance. Commentators have suggested that *BD Inns* does not settle the matter. See California Real Property Remedies and Damages §§5.28-5.32 (2d ed Cal CEB 2002). At the very least, the seller must allege contrary facts to plead claims for specific performance and general damages under §3307 in the alternative. For the former, the seller must plead that monetary damages are not available, because the value of the property equals the contract price; but for the latter, the seller must plead that the value of the property is below the contract price.

Second, the seller must remain ready to convey the property to the buyer until the action is concluded and must be able to convey good title to the buyer. CC §3394. Most sellers prefer to remarket the property rather than wait for the time required to reach trial in the hope of a judgment requiring the buyer to purchase it.

Most sellers agree to waive all remedies other than liquidated damages. In a rising market, sellers wish to be paid the amount of the liquidated damages and be free to take advantage of the increase in values. In a falling market, sellers often wish to sell the property as soon as possible rather than to risk further losses if the specific performance action is not successful.

© The Regents of the University of California

C. Buyer's Remedies

§4.144 1. Damages

The buyer may recover general damages if the seller fails to convey the property under CC §3306, special damages for other breaches of the agreement under CC §3300, and damages for fraud and misrepresentation. These remedies are available as a matter of law. The issues in negotiating a purchase agreement are whether the buyer's right to damages should be waived, limited, or liquidated. See form 4.177-4.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.145 a. Civil Code §3306

§4.145 a. Civil Code §3306

Damages for the seller's failure to convey the property under CC §3306 include the following:

- The price paid;
- The difference between the contract price and the value of the property at the time of the breach (see *Reese v Wong* (2001) 93 CA4th 51, 112 CR2d 669);
- Expenses incurred in examining title and preparing "the necessary papers";
- Expenses incurred in "preparing to enter upon the land";
- Consequential damages, subject to the customary requirement of foreseeability (lost profits are usually not available); and
- Interest.

Obviously, the remedy is much more useful to a buyer in a rising market. The availability of prejudgment interest is subject to CC §3287. See California Real Property Remedies and Damages §§4.12-4.28 (2d ed Cal CEB 2002).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.146 b. Civil Code §3300

§4.146 b. Civil Code §3300

Damages for breaches of the agreement by the seller (other than seller's failure to convey property; see §4.146) are available under CC §3300. These include breaches of covenants, indemnities, representations, or warranties in the agreement. Examples include defective title despite a title warranty, failure to complete construction on the property, failure to remove a mechanic's lien, or a physical condition of the property that is contrary to a representation. The damages must be reasonably foreseeable. See California Real Property Remedies and Damages §§12.17-12.19 (2d ed Cal CEB 2002).

© The Regents of the University of California

§4.147 c. Fraud and Misrepresentation

In the event of the seller's fraud or misrepresentation, the buyer can elect to affirm the contract and sue for damages under CC §3343 or to rescind the contract and seek damages under CC §1692. These claims may be pleaded in the alternative. Damages under §3343 include the difference between the contract price and the value of the property and any consequential damages. Consequential damages and interest may be sought in addition to rescission. Both causes of action can support a claim for punitive damages. See California Real Property Remedies and Damages §§3.11-3.60 (2d ed Cal CEB 2002).

© The Regents of the University of California

§4.148 2. Methods to Limit Buyer's Damages

Sellers sometimes seek to limit the buyer's broad remedies for damages by limiting the amount of damages available or seeking a waiver of damages claims altogether. Some agreements set a maximum amount of damages for which the seller can be liable, and others simply liquidate the amount of damages. Civil Code §1671(d) permits provisions liquidating the buyer's damages for the seller's breach. Sellers often seek to limit damages for breaches of representations and warranties by limiting the time the representations and warranties survive closing and the amount of damages that can be recovered. See discussion in §4.107, and form 4.173-4. Yet another technique sellers sometimes use to eliminate damages as a remedy is to include a provision limiting the buyer's remedies to either termination of the agreement with return of deposits or specific performance.

© The Regents of the University of California

§4.149 3. Specific Performance

Specific performance is available to the buyer for the seller's default unless it is excluded by the purchase agreement. See, *e.g.,* form 4.177-4, Alternative 2. Buyers usually resist strongly any attempt by sellers to restrict or eliminate the buyer's right to specific performance. Limitations usually give the seller means to avoid the contract. The remedy will be available subject to CC §§3384-3395 and the extensive case law on specific performance. See California Real Property Remedies and Damages, chap 5 (2d ed Cal CEB 2002).

A provision liquidating the seller's damages will not prevent the buyer from compelling specific performance of the contract. In *Bleecher v Conte* (1981) 29 C3d 345, 213 CR 852, the buyers had sought specific performance against the sellers, who argued that, because the liquidated damages provision prevents the seller from obtaining specific performance against the buyer, there was no mutuality of obligation. The court disagreed, saying that there was mutuality of obligation and that CC §3386 eliminated any requirement for mutuality of remedy. See form 4.177-4, Alternative 1.

Specific performance is available to a nondefaulting buyer even if the property is being purchased for investment purposes. See *Real Estate Analytics, LLC v Vallas* (2008) 160 CA4th 463, 476, 72 CR3d 835 (each parcel of land is presumed to be unique; nonbreaching buyer of commercial investment is entitled to specific performance unless defaulting seller rebuts presumption that monetary damages are inadequate to compensate buyer). In *Peak-Las Positas Partners v Bollag* (2009) 172 CA4th 101, 90 CR3d 775, the court affirmed a judgment extending escrow on a land sale contract so the buyer could obtain a lot line adjustment, finding that the seller had acted unreasonably in denying consent to an escrow extension and had breached the purchase contract. An amendment to the purchase contract extended the close of escrow for 5 years and provided for future escrow extensions by mutual consent of the buyer and seller, not to be unreasonably withheld or delayed. The buyer had paid 98 percent of the purchase price and spent $5 million in project costs and was diligent in trying to obtain the lot line adjustment.

A court has power to award compensation incidental to a decree of specific performance. Both the seller and buyer are entitled to receive full performance of the contract when specific performance has been granted. When a buyer is deprived of possession of the property pending resolution of the dispute and seller receives rents and profits, the buyer is entitled to a credit against the purchase price for the rents and profits from the time the property should have been conveyed to the buyer. A seller is entitled to receive the value of seller's lost use of the purchase price during the period performance was delayed. *Stratton v Tejani* (1982) 139 CA3d 204, 187 CR 231. See, however, *Kassir v Zahabi* (2008) 164 CA4th 1352, 80 CR3d 1 (seller not entitled to interest on sale proceeds if property was overencumbered because entire purchase price would have been used to pay off existing liens).

For a discussion of the availability of lis pendens after filing an action for specific performance, see California Real Property Remedies and Damages, chaps 5, 13 (2d ed Cal CEB 2002).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.150 D. Alternative Dispute Resolution

§4.150 D. Alternative Dispute Resolution

Alternative dispute resolution (ADR) is the name given to any method of resolving a dispute outside a courtroom, thus allowing the parties to avoid the often excessive expense and delay of standard litigation. The ADR process is less cumbersome than standard litigation because many of the rules of civil procedure, including discovery, evidence, hearsay, and even due process and appeal, are suspended or waived. Although there are many methods and combinations of ADR, it generally falls into one of two categories, depending on whether the results are binding on the parties (*i.e.,* whether the parties have recourse to standard litigation if they do not like the ADR result). Arbitration is generally binding on the parties, while mediation is not. On ADR generally, see A Litigator's Guide to Effective Use of ADR in California (Cal CEB 2005).

NOTE: Despite the name "judicial arbitration" given to court-ordered or court-sanctioned ADR, it actually takes the form of mediation. In the authors' experience, mediation provisions are seldom included in purchase and sale agreements and mediation is only used if it is required by the court under local rules or CCP §§1775-1775.15.

In mediation, the parties agree to suspend their rights and, if they do not like the result, they can resort to traditional litigation with all its rules of civil procedure. In arbitration, the parties waive many of the protections of the rules of civil procedure and agree to be bound by the third party arbitrator's decision. The grounds for challenging a petition to confirm an arbitration award are very narrow. CCP §§1286-1286.6.

Parties cannot be forced to arbitrate; and they must agree in writing to arbitrate. CCP §1297.72. Usually, the agreement to arbitrate is entered into before a dispute arises and is just one provision in a larger contract. See CCP §1297.71.

Specific language must be used to create an enforceable binding arbitration provision in most contracts to convey real property, including purchase and sale agreements and leases with options to buy (but no deeds of trust containing a power of sale) and in related contracts with agents. CCP §1298(a)-(b). Arbitration provisions in such contracts must be clearly titled "ARBITRATION OF DISPUTES." CCP §1298. If the contract is printed, the title must be in at least 8-point bold type or in contrasting red in at least 8-point type; if the contract is typed, the title must be in capital letters. CCP §1298(b). In addition to the required title, CCP §1298(c) requires that specific notice language be set forth in the same size type as required for the title. The statutory language is set forth in section 9.5.2 of form 4.177-5. Immediately following such notice language, a line or a space must be provided for the parties to indicate their assent or nonassent to the arbitration provision. CCP §1298(c). Arbitration provisions in purchase and sale agreements are enforceable only when signed by the buyers and sellers. *Marcus & Millichap Real Estate Inv. Brokerage Co. v Hock Inv. Co.* (1998) 68 CA4th 83, 80 CR2d 147 (buyer initialed arbitration provision in purchase agreement, but seller did not; broker representing both parties, sued by buyer for negligent misrepresentation, could not compel parties to arbitrate). A contract fraudulently executed is void and an arbitration clause in a void contract is unenforceable. A contract fraudulently induced, however, is voidable and an arbitration clause in a voidable contract is enforceable and parties must arbitrate even though the contract was fraudulently induced. *Rosenthal v Great W. Fin. Sec. Corp.* (1996) 14 C4th 394, 58 CR2d 875.

PRACTICE TIP: Although attorneys differ on the merits of arbitration, when sellers are foreign entities, there is a compelling reason to include an arbitration provision. Currently, there is no international treaty permitting enforcement of United States judicial decisions in foreign countries. Thus, if a foreign seller breaches a warranty and the buyer is awarded damages in court, that award is not automatically enforceable. A second action must then be brought in the foreign jurisdiction. Under the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (June 10, 1958), commonly known as the New York Convention and signed by many countries, arbitration awards are enforceable in foreign jurisdictions. Enforcement is often subject to limitations set out in the local laws under which the New York Convention was adopted. Attorneys should consult with counsel in the foreign jurisdiction for any such limitations.

For a dispute resolution form providing for arbitration, see form 4.177-5. For a complete discussion of alternative dispute resolution for real property actions, see California Real Property Remedies and Damages, chap 14 (2d ed Cal CEB 2002).

© The Regents of the University of California

XIII. MISCELLANEOUS PROVISIONS

§4.151 A. Notices

The agreement should include a provision listing the notice addresses for both parties (with any courtesy copy addresses) and the escrow holder. All notices should be required to be in writing to ensure that there is a record of them and to avoid disputes about their contents. It is essential that the agreement provide the acceptable methods for notice and a statement of when the notice will be effective. Certified mail or an overnight delivery service with a return receipt is useful—and even superior to personal service—to establish that the party to whom the notice was sent received it, and to verify the date of receipt. If the parties agree that notices can be sent by facsimile transmission, the provision should require that a confirmation copy be sent by mail. Agreements often state that a facsimile notice is effective when received if confirmed by mail. If it is not effective until receipt of the confirmation copy delivered by mail, then using this method of notice has no particular advantage.

If an agreement does not define "notice," certain statutes may produce unintended results:

- Constructive notice of a fact exists upon "actual notice of circumstances sufficient to put a prudent man upon inquiry as to a particular fact." CC §§18-19.
- A correctly addressed and properly mailed letter is presumed to have been received in the ordinary course of mail. Evid C §641.

PRACTICE TIP: Notice provisions may state that a copy be sent to a party's attorney. A "copy to" provision may not be good practice. First, if notice is provided to a party but not to the attorney, the notice may be ineffective. Second, the language arguably imposes obligations on the attorney with respect to a client the attorney no longer represents. Also, if the attorney moves, must the attorney send a change of address to all parties affected by a notice clause? A "courtesy copy" notice provision may serve as an acceptable alternative.

See form 4.178-1.

© The Regents of the University of California

§4.152 B. Time Is of the Essence

A "time is of the essence" provision printed on a form may have little value. Generally, California courts do not tend to strictly enforce these provisions, but look at whether the parties actually intended to strictly restrict a party's performance or merely used boilerplate language, whether the delay was material, and what the defaulting party's loss would be as a result of the forfeiture of contract rights compared with the loss the nondefaulting party would sustain as a result of the delay. See *Fowler v Ross* (1983) 142 CA3d 472, 479, 191 CR 183; *Nash v Superior Court* (1978) 86 CA3d 690, 696, 150 CR 394, disapproved on other grounds in *Malcolm v Superior Court* (1981) 29 C3d 518, 528 n5, 174 CR 694; *Williams Plumbing Co. v Sinsley* (1975) 53 CA3d 1027, 126 CR 345.

Courts may also decide not to strictly enforce a "time is of the essence" clause because money damages usually compensate the parties for any harm resulting from delayed performance. However, a "time is of the essence" provision is sometimes given effect. In *Pittman v Canham* (1992) 2 CA4th 556, 3 CR2d 340, the buyer sued the seller for breach of contract in failing to complete the transaction. Neither party had tendered performance by the date set forth in the contract and the escrow instructions. Both documents stated that time was of the essence. The court held that, because of that provision, the failure of both parties to complete the concurrent conditions on time resulted in termination of the contract. But see *Ninety Nine Invs., Ltd. v Overseas Courier Serv. (Singapore) Private, Ltd.* (2003) 113 CA4th 1118, 1133, 6 CR3d 891, distinguishing *Pittman* and concluding it is "an aberration in the facts," and 1 Miller & Starr, California Real Estate §1:162, p 688 (3d ed 2000).

NOTE: A court of appeal has held that CCP §12a, which extends the time for performance of an act provided or required by law, does not apply to acts governed solely by contractual provisions. *Gans v Smull* (2003) 111 CA4th 985, 4 CR3d 353.

Some deposit receipts contain language permitting the broker to extend time, and escrow instructions often direct the escrow agent to close escrow as soon as possible after the closing date. Courts usually have held that the parties have waived the "time is of the essence" provision by failing to include such provisions in the agreement or escrow instructions. *Katemis v Westerlind* (1953) 120 CA2d 537, 261 P2d 553. Either party may waive strict performance by the other merely by failing to insist on it. *Johnson v Goldberg* (1955) 130 CA2d 571, 279 P2d 131. Either party may also waive a "time is of the essence" provision by continuing to deal with the other party after the date specified in the contract and not establishing a new time requirement. *Galdjie v Darwish* (2003) 113 CA4th 1331, 7 CR3d 178. See 1 Miller & Starr, California Real Estate §2:24 (3d ed 2000) for a discussion of "time is of the essence" provisions.

In some circumstances, a client will suffer specific damages if the transaction is not closed in a timely manner. Specifying precisely what those damages will be provides a stronger position to argue for enforceability of the provision. If the seller wants to be able to enforce a right to terminate if escrow does not close by a specified date, the purchase agreement must state this right specifically and unequivocally, and the seller must continue to insist on timely performance throughout the escrow period; take no action inconsistent with this position; and be prepared to tender performance before declaring a default.

The effectiveness of a provision permitting one party to withdraw from escrow against the will of the other depends on the attitude of the escrow holder, which is traditionally cautious. After an alleged breach, escrow holders almost universally refuse to return money and documents in escrow unless all parties consent in writing.

PRACTICE TIP: "Time is of the essence" should be included when one party's failure to perform timely is intended to excuse the other party's performance. Otherwise "time is of the essence" can backfire by releasing all parties from their obligations when concurrent performances are required.

See form 4.178-9.

© The Regents of the University of California

§4.153 C. Attorney Fees

Most California contracts include a prevailing-party attorney fees provision, as permitted by CC §1717. Attorney fees are not recoverable by the prevailing party in a contract action unless the contract expressly so provides. CCP §1021. They may, however, be awarded to the prevailing party even if the contract purports to award them only to one party. CC §1717. The example in form 4.178-10, in addition to providing for attorney fees between the parties, provides for attorney fees for the prevailing party when the escrow holder interpleads funds. For discussion of attorney fees sought by the broker, see §2.152.

NOTE: An attorney fee provision between the buyer and the seller in a purchase and sale agreement cannot be enforced by the buyer against an intervening non-bona-fide buyer from the seller, against whom the original buyer brings a successful specific performance action. *Glynn v Marquette* (1984) 152 CA3d 277, 199 CR 306 (intervening buyer, although properly a defendant in specific performance action (CC §3395), was not a party to original purchase and sale agreement and did not assume obligations of agreement).

Contract language permitting recovery of fees "in any action or proceeding arising out of this agreement" can permit recovery of fees as costs in a tort, as well as in a contract action. *Lerner v Ward* (1993) 13 CA4th 155, 16 CR2d 486. In *Lerner*, the parties included the language quoted above in their purchase agreement. In a later lawsuit against the sellers, the buyers dismissed their contract claims and proceeded solely on a fraud cause of action. The buyers lost their case, and the sellers sought fees. The trial court denied fees, and the appellate court reversed. Because no contract claim was made, the court could not award fees under CC §1717. Nevertheless, because the tort cause of action for fraud arose from the written agreement and because the parties had agreed to award fees to the prevailing party in actions arising from the agreement, the sellers were entitled to attorney fees as costs under that agreement. See CCP §1021 (attorney fees based on parties' agreement). See also *Santisas v Goodin* (1998) 17 C4th 599, 71 CR2d 830; *Allstate Ins. Co. v Loo* (1996) 46 CA4th 1794, 54 CR2d 541.

NOTE: Code of Civil Procedure §1021 has no reciprocal provision, as does CC §1717, under which, if the contract provides for attorney fees to one party, the other party is entitled to its fees if it is the prevailing party. Consequently, if the action is in tort, §1021 cannot be the basis of a claim for attorney fees by a prevailing party if the contract does not specifically provide for attorney fees to that party. *Moallem v Coldwell Banker Commercial Group, Inc.* (1994) 25 CA4th 1827, 31 CR2d 253.

If a case is dismissed at the pretrial stage, the parties must bear their own attorney fees for contract claims, even if the purchase agreement has a provision awarding attorney fees to the prevailing party.

PRACTICE TIP: The parties should define any of the following terms used in the attorney fees provisions "prevailing party," "court having jurisdiction," and "attorney fees and costs."

© The Regents of the University of California

§4.154 D. Waiver

Unless otherwise provided, the law may imply waiver when a party entitled to performance accepts partial or defective performance. 1 Witkin, Summary of California Law, *Contracts* §817 (10th ed 2005). Similarly, because many of the remedies available in a breach are inconsistent, the law may find that the injured party elected to pursue one remedy to the exclusion of others. The parties can modify or nullify the doctrine of election of remedies by contract. 3 Witkin, California Procedure, *Actions* §196 (4th ed 1996). To avoid a broader waiver than intended or an early election of remedies, a provision stating that waivers must be in writing and limiting the effect of waivers should be included in the agreement. See form 4.178-3.

© The Regents of the University of California

§4.155 E. Assignment by Buyer

An agreement is assignable by law unless it was intended to be nonassignable or an assignment would impair the seller's chances of obtaining the buyer's performance. *Farmland Irrig. Co. v Dopplmaier* (1957) 48 C2d 208, 308 P2d 732. If the parties wish to limit the agreement's assignability, the agreement should so state. An assignor is not relieved of liability unless the agreement so specifies. CC §1457. Thus, unless the assigning buyer is specifically released, the seller can look to the assigning buyer if the assignee fails to perform.

A formal written assignment should be executed between the buyer and the assignee to ensure that the rights to specific enforcement of the agreement are transferred to the assignee.

For a form allowing buyer to assign on notice to seller, see form 4.178-11.

© The Regents of the University of California

§4.156 1. Entity to be Formed

If the buyer intends to form a corporation, partnership, or other entity to take title, or if the buyer wishes to sell to another, the buyer will want the right to assign the agreement without further consent of the seller. As discussed in §4.157, merely stating "buyer or nominee" in the agreement is inadequate because this description of the buyer is not sufficiently certain. Instead, the buyer should seek a broad right to assign. The seller who wants a more restrictive provision should add to the agreement clauses that (a) require the buyer to hold a specified interest in the assignee and (b) state that the buyer is not relieved of the agreement's obligations until escrow closes. The seller may also require the right to approve the assignee; for example, if the seller is taking back a note for all or part of the purchase price, the seller will want to know the buyer's identity and credit standing.

Often a purchase agreement is executed by a promoter or by an agent of an undisclosed principal in the expectation that an entity will be formed by the principal or the party ultimately buying the property to take title. If there is no misrepresentation by the signator, the seller is apparently bound to perform, but the assignment provision should expressly permit the assignment. If the agreement is executed in the name of a corporation that has yet to be formed rather than in an agent's name, however, the seller can probably withdraw from the transaction before the corporation is formed. See *Macy Corp. v Ramey* (Ohio CP 1957) 144 NE2d 698. This may also be true if the agreement is executed by a limited partnership or a limited liability company that is not yet in existence because of a failure to comply with the requirements for forming a limited partnership in Corp C §15621 (Corp C §15902.01, operative Jan. 1, 2008, for new or electing limited partnerships) or a limited liability company in Corp C §17050.

When the actual buyer is an entity to be formed, the promoter or agent should complete its formation before the close of escrow for the following reasons:

- The entity can take title as a grantee (and avoid the need for a subsequent transfer of title, which would complicate obtaining title insurance for the actual buyer);
- If the promoter or agent takes title and later conveys to the new entity, the property will be exposed to the promoter's or agent's personal creditors;
- A transfer of title might trigger a due-on-sale provision in an encumbrance; and
- A transfer of title could cause a property tax reassessment or incur a transfer tax.

© The Regents of the University of California

§4.157 2. Use of Nominees

Although it is relatively common for a buyer to include a reference to an unnamed "nominee" as an alternative purchaser, the author strongly advises against such practice. A provision that allows the party signing the purchase agreement as buyer to designate a nominee is not a satisfactory way of facilitating a transfer to the actual buyer, because the actual buyer, even after being designated the nominee, is not entitled to specific enforcement of the agreement against the seller. In *Cisco v Van Lew* (1943) 60 CA2d 575, 141 P2d 433, the court concluded that the agreement was uncertain because no memorandum signed by the seller identified the buyer. The court also decided that mere designation of a nominee without a formal assignment did not vest in the nominee (in this case the principal) any right to enforce the agreement and that, without an assumption by the assignee of the buyer's obligations under the agreement, the agreement lacked the mutuality of obligation required for specific performance. See also *Ott v Home Sav. & Loan Ass'n* (9th Cir 1958) 265 F2d 643 ("nominee" not a synonym for "assignee"); *Rivadell, Inc. v Razo* (1963) 215 CA2d 614, 30 CR 622. But see *JMR, Inc. v Hedderly* (1968) 261 CA2d 144, 148, 67 CR 742, in which the court concluded that a corporate nominee should have the opportunity to present evidence "to show that the contract was made in the contemplation of the formation of the plaintiff corporation, and for its benefit, and that it adopted and ratified the contract after its formation."

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.158 F. Interpretation of Agreement

§4.158 F. Interpretation of Agreement

Several provisions in an agreement set out the agreed rules of interpretation to be used in construing the agreement. One such provision is intended to negate the usual rule (CC §1654) that a document is interpreted against the party who caused the uncertainty to exist. Choice-of-law provisions for contracts among residents of different states for California property usually choose California law (as permitted by CC §1646.5), but exclude the California choice-of-law rules to avoid any interpretation that could lead to the choice of another state's law. See form 4.178-7. Another common provision requires that all amendments be in writing.

PRACTICE TIP: Specific language is also important to clearly document the parties' intent. The following drafting suggestions can help avoid ambiguity in the agreement:

- The word "or" creates mutually exclusive options, but can mean "and." Parties usually intend "or" to mean both "and" and "or." Careful drafting can clarify the parties' intent.
- "Including," in the phrase "including but not limited to" is clearer than "including" alone, which can limit whatever is described to the examples given.
- An easy drafting solution is to state that "or" is not exclusive and "including" is not limiting.

Drafters should avoid using the language, "all parties have participated in the … drafting of this Agreement" if one party has not in fact fully participated. Use the following instead: "Any rule of construction to the effect that ambiguities are to be resolved against the drafting party will not apply in interpreting this Agreement."

© The Regents of the University of California

§4.159 1. Integration Provision

In the absence of fraud, lack of consideration, and similar defenses, an integration provision expresses the parties' intent to terminate all agreements not set forth in the document in order to eliminate any claim that other agreements exist outside the document. Requiring that all amendments be in writing satisfies the Statute of Frauds and establishes a record of the amendments made. This provision makes extrinsic evidence to vary its terms inadmissible. CCP §1856. Note, however, that despite such a provision courts have been lenient in admitting extrinsic evidence to interpret ambiguities. See 2 Witkin, California Evidence, *Documentary Evidence* §§74-85 (4th ed 2000). See form 4.178-2.

Although the integration clause is designed to invoke the parol evidence rule, it is not conclusive proof of an integrated agreement. The terms of a "final" expression of agreement may be explained by evidence of consistent additional terms. CCP §1856(a)-(b); Com C §2202(b).

An integration provision should include the phrase "complete and exclusive statement" to duplicate the parol evidence rule. See CCP §1856 and Com C §2202 (a writing intended as a "complete and exclusive" statement of the terms of the agreement may not be explained or supplemented even by evidence of consistent additional terms).

Agreements that include an integration provision should incorporate supporting documents, such as schedules, riders, and exhibits, and provide that (1) no party has been induced to enter into the agreement by any representation or warranty outside those expressly set forth, and (2) no party is relying on such representation or warranty.

© The Regents of the University of California

§4.160 2. Counterparts

Because the parties are often in a hurry to execute the agreement, using counterparts allows simultaneous execution without requiring all parties to meet. Counterparts, however, increase the possibility of unauthorized alteration of the document because not all parties sign the same document at the same time. To reduce the chances of alteration, each party should execute a complete agreement, not just the signature page. This procedure makes it more difficult to insert a substituted page, and, if the counterparts are later found not to match, it will establish which party signed what form of the document. See form 4.178-14.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.161 3. Binding on Successors

§4.161 3. Binding on Successors

Agreements customarily include provisions stating that the agreement survives the death of a party or assignment of the agreement. The usual rule is that a contractual obligation survives the death of the promisor except for a contract calling for personal services by the promisor. 1 Witkin, Summary of California Law, *Contracts* §838 (10th ed 2005). Depending on the particular agreement, a court might or might not find a purchase and sale agreement to be for personal services. See, *e.g., Central Contra Costa Sanitary Dist. v National Sur. Corp.* (1952) 112 CA2d 61, 246 P2d 150. The provision should be limited if the agreement is not freely assignable. See form 4.178-11.

© The Regents of the University of California

§4.162 G. Amendments Only in Writing

Generally, only a contract in writing or an oral executed agreement can modify a written contract. However, an oral agreement with new consideration can modify a written contract, and an oral agreement without new consideration can modify a contract for the sale of goods. If the parties wish to preclude later oral modifications, they should include a provision requiring a writing. CC §1698.

The provision, however, may not apply to a fully executed modification. For example, a subcontractor can enforce an oral agreement for extra work after the work is done, even though the contract required the agreement for extra work to be in writing. Nor will the provision apply to an oral novation, an oral rescission, an oral waiver, or when the party attempting to enforce the prohibition is estopped from doing so. CC §1698.

See form 4.178-3.

© The Regents of the University of California

§4.163 H. No Third Party Benefit

A third party may enforce in its own name an unrescinded contract expressly made for the third party's benefit. A third party may sue the promisor, the promisee, or both. The contract need not specifically name the beneficiary as long as he or she is a member of the class identified. See, *e.g., Prouty v Gores Technol. Group* (2004) 121 CA4th 1225, 18 CR3d 178 (employees deemed third party beneficiaries and had right to recover severance benefits under contract from parent company and present owner).

The intent to make the contract expressly for the third party's benefit must appear from the contract and the circumstances surrounding its formation. For example, business creditors are third party beneficiaries of contracts in which business liabilities are transferred, and an agreement that expressly provides for payment to a third party is made for the benefit of that party. Therefore, if the parties want to make clear that the contract is not intended to benefit any third parties, it should clearly say so. See form 4.178-12.

© The Regents of the University of California

§4.164 I. Severability

Whether a contract is severable or entire depends on the parties' intentions, set forth in the language of the contract and the surrounding circumstances. In a severable contract, separate partial performances by one party are agreed to be exchanged for partial performances by the other. The failure of a party to perform one part of the contract does not bar that party from recovering for performance of another part. In an integrated contract, all performances are common and interdependent, and any material breach justifies termination of that contract.

See form 4.178-4.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.165 J. Tax-Deferred Exchange

§4.165 J. Tax-Deferred Exchange

A delayed exchange provision (IRC §1031) is included in form 4.178-15. For discussion of tax-deferred exchanges, see §§1.119, 4.127. For a comprehensive treatment of the requirements and tax consequences of a tax-deferred exchange, see Real Property Exchanges (3d ed Cal CEB 2002).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.166 XIV. PURCHASE AND SALE AGREEMENT

§4.166 XIV. PURCHASE AND SALE AGREEMENT

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§4.166-4.182.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

This buyer-oriented purchase and sale agreement assumes that the property being sold is a commercial building with both office and retail tenants. Some seller alternatives are also provided. As with any form, the provisions of this form must be adapted to the circumstances of the particular transaction.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.167 A. Form: Title and Introductory Paragraph

§4.167 A. Form: Title and Introductory Paragraph

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§4.166-4.182.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

4.167-1 Title and introductory paragraph

PURCHASE AND SALE AGREEMENT

This Purchase and Sale Agreement (Agreement) is made as of _ _[*date*]_ _ (Effective Date), between _ _[*name*]_ _, a _ _[*type of entity*]_ _ (Seller), and _ _[*name*]_ _, a _ _[*type of entity*]_ _ (Buyer).

Comment: On parties to the agreement, see §§4.14-4.28; on the preamble to the agreement, see §4.29.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.168 B. Form: Recitals

§4.168 B. Form: Recitals

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§4.166-4.182.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

4.168-1 Recitals

RECITALS

A. Seller is the owner of certain real property located in the City of _ _[*name*]_ _ (City), County of _ _[*county*]_ _ (County), State of California (State), consisting of a _ _[*number*]_ _-acre parcel of land, commonly known as _ _[*address*]_ _, _ _[*city*]_ _, California, with Assessor's parcel number_ _[*number*]_ _, which is more particularly described in Exhibit A (Land), and the related improvements, appurtenances, and certain related personal and intangible property.

B. The Land is improved by a _ _[*number*]_ _-story building located at _ _[*address*]_ _, _ _[*city*]_ _, California (Building), containing approximately _ _[*number*]_ _ square feet. There are approximately _ _[*number*]_ _ office tenants in the Building and _ _[*number*]_ _ retail tenants on the ground floor.

C. Seller desires to sell and Buyer desires to purchase the Property, including the Land and the Building, as specifically described below.

Comment: On the advantages of using recitals, see §4.29.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.169 C. Form: Agreement of Sale

§4.169 C. Form: Agreement of Sale

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§4.166-4.182.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

4.169-1 Agreement of sale

ARTICLE 1

AGREEMENT OF SALE

1.1. Purchase and Sale. For good and valuable consideration, the receipt and adequacy of which are hereby acknowledged, Seller agrees to sell and Buyer agrees to purchase all Property described below in _ _[*e.g., section 1.2*]_ _, under the terms and conditions of this Agreement.

4.169-2 Description of property

1.2. Description of the Property. The property to be sold and purchased under this Agreement (Property) consists of the following:

1.2.1. Land. As described in Recital A.

1.2.2. Appurtenances. All privileges, rights, easements appurtenant to the Land, including without limitation all minerals, oil, gas, and other hydrocarbon substances on and under the Land; all development rights, air rights, water, water rights, and water stock relating to the Land; all right, title, and interest of Seller in and to any streets, alleys, passages, water and sewer taps, sanitary or storm drain capacity or reservations and rights under utility agreements, and other easements and other rights-of-way included in, adjacent to, or used in connection with the beneficial use and enjoyment of the Land (collectively, the Appurtenances).

1.2.3. Improvements. The Building described in Recital B and all other buildings, structures, fences, parking areas, or improvements located upon the Land or upon the Improvements, including fixtures, systems, and equipment attached to the Land or Improvements and used in connection with the operation or occupancy of the Land and Improvements (such as heating and air-conditioning systems, refrigeration, ventilation, garbage disposal, or utility conduits) (collectively, the Improvements, which together with the Land and the Appurtenances are called the Real Property).

1.2.4. Personal Property. Certain tangible personal property and all intangible property owned by Seller that is located on or in or is used in connection with the use or operation of any of the Property (Personal Property). Personal Property must include, without limitation, all the following: (a) all of the tangible property listed on a schedule to be delivered according to _ _[*e.g., section 3.1.3*]_ _ of this Agreement; (b) the service contracts listed on a schedule to be delivered according to _ _[*e.g., section 3.1.3*]_ _ of this Agreement, which Buyer elects to assume, by written notice to Seller not less than _ _[*e.g., 10*]_ _ days before the Closing; (c) all rights under the Leases (defined in _ _[*e.g., section 3.1.8*]_ _); (d) all warranties and guaranties on or related to the tangible Personal Property or related to construction, repair, or alteration work on the Real Property, to the full extent such warranties and guaranties are assignable; (e) all licenses and permits related to the Property; (f) all plans, drawings, engineering studies located within, used in connection with, or related to the Property; (g) all intellectual property associated with, related to, or used in connection with the Property, including logos, trademarks, designs, tradenames, service marks, e-mail addresses, domain names, and telephone numbers; and (h) all goodwill associated with the Real Property.

Comment: On consideration, see §4.11; on the necessity of mutual agreement, see §4.30; on description of property, see §§4.31-4.34.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.170 D. Form: Purchase Price

§4.170 D. Form: Purchase Price

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§4.166-4.182.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

4.170-1 Amount

ARTICLE 2

PURCHASE PRICE

2.1. Amount. The full purchase price (Purchase Price) for the Property is _ _[*amount*]_ _ Dollars (_ _[*dollar amount*]_ _), and is payable in accordance with this _ _[*e.g., Article 2*]_ _.

4.170-2 Deposits

2.2. Deposits.

2.2.1. Initial Deposit. Within _ _[*e.g., 3*]_ _ Business Days after the Effective Date, as a deposit against the Purchase Price, Buyer must deposit _ _[*dollar amount*]_ _ (Initial Deposit) into an escrow (Escrow) to be opened with _ _[*name*]_ _ (Escrow Holder).

2.2.2. Second Deposit. On the Contingency Date (as defined in _ _[*e.g., section 3.2*]_ _), if the contingencies set forth in _ _[*e.g., Article 3*]_ _ have been met and this Agreement has not been otherwise terminated, Buyer must deposit _ _[*dollar amount*]_ _ into Escrow as an additional deposit against the Purchase Price (Second Deposit).

2.2.3. Requirements for Deposit. Buyer may make the Initial Deposit and the Second Deposit (collectively, the Deposit) in cash, or by check payable to the Escrow Holder, or by electronic transfer of federal funds. The Escrow Holder will hold the Deposit in an escrow account at a bank and invested in investments approved by Buyer, with interest accruing for the benefit of Buyer. On the Closing Date (defined in _ _[*e.g., section 7.2.2*]_ _), the Deposit will be credited against the Purchase Price and paid to Seller. If this Agreement terminates for any reason except Buyer's default, the Escrow Holder must refund the Deposit to Buyer.

2.2.4. Option to Substitute Letter of Credit. Buyer has the right, at its option, to substitute a letter of credit (Letter of Credit) for all or any portion of the Deposit. The Letter of Credit must be drawn on a reputable bank with an office in _ _[*city*]_ _, California (Issuing Bank), reasonably acceptable to Seller and must name Escrow Holder as the beneficiary. The Letter of Credit must provide that Buyer may not revoke, cancel, or otherwise modify the Letter of Credit. The Letter of Credit may not impose any conditions to the drawing thereof other than a certificate from the Escrow Holder that Escrow Holder is entitled to draw on the Letter of Credit under this Agreement. The maturity date of the Letter of Credit must be at least _ _[*e.g., 45*]_ _ days after the expected Closing Date. If Buyer does not renew or extend the Letter of Credit at least _ _[*e.g., 30*]_ _ days before the maturity date, Escrow Holder must draw down the proceeds of the Letter of Credit. Escrow Holder may not otherwise draw on the Letter of Credit until Escrow Holder is authorized to deliver the Deposit under the terms of this Agreement. If Escrow Holder draws down the Letter of Credit, it must hold all proceeds as the Deposit or as a portion of the Deposit. If, at or before the Closing, Buyer places, or causes to be placed, good and immediately available funds into Escrow to fully replace the Letter of Credit, then Escrow Holder must return the Letter of Credit to Buyer, and the proceeds of the Letter of Credit will not be credited against the Purchase Price.

4.170-3 Assumption of note secured by deed of trust

2.3. <u>Assumption of Note Secured by Deed of Trust.</u> Buyer's purchase of the Property is subject to Buyer's assumption of that certain deed of trust dated _ _[*date*]_ _, in favor of _ _[*beneficiary's name*]_ _, recorded on _ _[*date*]_ _, as Instrument _ _, in book _ _, page _ _ of _ _[*identify records*]_ _, in the Office of the County Recorder of _ _[*name*]_ _ County, securing a note with an approximate current unpaid balance of _ _[*dollar amount*]_ _ (Assumed Loan). Buyer will be credited with the balance of the principal owed under the Assumed Loan on the Closing Date.

4.170-4 Seller financing

2.4. <u>Seller Financing.</u> Buyer agrees to deliver to Seller through Escrow at Closing Buyer's promissory note secured by a deed of trust in favor of Seller in the principal amount of _ _[*dollar amount*]_ _ (Seller Financed Amount), bearing interest in the amount of _ _[*number*]_ _ percent per year from the Closing Date, payable in _ _[*number*]_ _ installments of _ _[*dollar amount*]_ _ beginning on _ _[*date*]_ _ and continuing until _ _[*date*]_ _, unless paid sooner (Seller Financing). The Seller Financed Amount will be credited against the Purchase Price on the Closing Date. The forms of promissory note and deed of trust to be delivered by Buyer at Closing are attached to this Agreement as _ _[*e.g., Exhibits B and C*]_ _.

4.170-5 Payment of balance

2.5. <u>Payment of Balance.</u> Buyer agrees to pay, or cause to be paid, the balance of the Purchase Price to Seller through the Escrow by depositing cash or a certified or cashier's check payable to the Escrow Holder, or by electronic transfer of federal funds, which must be delivered to the Escrow Holder at least _ _[*e.g., 1*]_ _ business day before the Closing Date.

4.170-6 Allocation of purchase price

[*If applicable, add the following option*]

[*Option: Allocation of purchase price*]

2.6. <u>Allocation of Purchase Price.</u> The Purchase Price will be allocated among various assets constituting the Property in accordance with an exhibit (Allocation of Purchase Price) to be negotiated by the parties in good faith, which exhibit will be prepared in the manner required by §1060 of the Internal Revenue Code of 1986 (Code), as amended, and attached to this Agreement as _ _[*e.g., Exhibit I*]_ _ to this Agreement at least _ _[*e.g., 5*]_ _ days before the Closing. Seller and Buyer agree to prepare and file all federal, state, local, and foreign tax returns and other filings reflecting this transaction on a basis consistent with such allocation, and to cooperate with each other in good faith in preparing any and all statements required to be included in their respective tax returns, including IRS Form 8594 and any required exhibits to the tax returns (or other forms required under §1060 of the Code, or other applicable tax laws) reflecting such allocation. Seller and Buyer further agree that they will not make any inconsistent written statement or take any inconsistent position on any tax returns, in any refund claim, or during the course of any Internal Revenue Service or other tax audit, so long as there exists a reasonable basis in law to maintain the position reflected by such allocation. Each party must notify the other party if it receives notice that the Internal Revenue Service or any other taxing authority proposes any allocation that is different from the allocation set forth on the Allocation of Purchase Price.

[*Continue*]

Comment: On purchase price and deposits, see §§4.35-4.44. On the parties' agreement allocating the purchase price, see §4.36.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.171 E. Form: Buyer's Contingencies

§4.171 E. Form: Buyer's Contingencies

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§4.166-4.182.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

4.171-1 Seller's delivery of documents

ARTICLE 3

BUYER'S CONTINGENCIES

[*Add one of the following alternatives*]

[*Alternative 1: Buyer's clause for seller's delivery of document*]

3.1. Seller's Delivery of Documents. Buyer's obligation to purchase the Property is expressly conditioned on Seller's delivering to Buyer all documents listed below (collectively, Preliminary Documents). Failure to deliver the Preliminary Documents within _ _[*e.g., 5*]_ _ days after the Effective Date will extend the Contingency Date (as defined in _ _[*e.g., section 3.2*]_ _) by 1 day for every 1 day thereafter that the last such Preliminary Document is delivered.

[*Alternative 2: Seller's clause for delivery of document*]

3.1. Seller's Delivery of Documents. Buyer's obligation to purchase the Property is expressly conditioned on Seller's making all documents listed below (collectively, Preliminary Documents) available to Buyer. On or before the _ _[*e.g., fifth (5th)*]_ _ day after the Effective Date, Seller must deliver directly to Buyer the Preliminary Report, the Rent Roll, the Leases, and the operating statements for the Property for the current year and the prior _ _[*e.g., 3*]_ _ years. Seller agrees to gather all other Preliminary Documents and make them available for inspection after the Effective Date during normal business hours at _ _[*address*]_ _.

[*Continue*]

3.1.1. Preliminary Report. A preliminary report (Preliminary Report) dated no earlier than _ _[*e.g., 30*]_ _ days before the Effective Date covering the Real Property and issued by _ _[*name*]_ _ (Title Company), together with a legible copy of all exceptions to title shown in the Preliminary Report, including each document, map, and survey referred to in the Preliminary Report.

3.1.2. Surveys. An ALTA survey of the Real Property, dated no earlier than _ _[*e.g., 60*]_ _ days before the Effective Date, meeting the requirements of the most current edition of the ALTA/ACSM Minimum Survey Standards (Survey) and showing Items _ _[*numbers*]_ _ from Table A of the ALTA/ACSM Minimum Survey Standards and copies of all other existing surveys in Seller's possession.

3.1.3. Schedules of Personal Property. A complete schedule of all tangible Personal Property to be sold under this Agreement and a complete schedule of all service contracts related to the Property that Seller does not intend to cancel before the Closing Date.

3.1.4. Agreements. Copies of all written easements, covenants, restrictions, agreements, service contracts, and other documents that affect the Property, including without limitation any agreements relating to insurance, service, operation, repair, supply, advertising, promotion, sale, leasing, or management of the Property or the use of the common facilities.

3.1.5. Licenses and Permits. Copies of any licenses, permits, or certificates required by governmental authorities in connection with construction or occupancy of the Improvements, including without limitation building permits, certificates of completion, certificates of occupancy, and environmental permits and licenses, and any correspondence related to the Improvements.

3.1.6. Plans. Copies of any existing construction drawings, as-built plans, and specifications for the Property.

3.1.7. Rent Roll. A rent roll, dated no earlier than _ _[*e.g., 10*]_ _ days before the Effective Date (Rent Roll).

3.1.8. Leases. Copies of all Leases (and any modifications or amendments to them) with all tenants of the Property (Leases), and any correspondence related to the Leases, including all statements from retail tenants of their sales.

3.1.9. Leasing Commission Agreements. A complete list of all agreements for leasing commissions payable on the Leases and renewals of or options on the Leases and copies of all such written agreements.

3.1.10. Tax Bills. Property tax bills for the past _ _[*e.g., 3*]_ _ years.

3.1.11. Financial Information. Copies of operating statements for the Property covering each calendar month of the current calendar year to date, and each of the prior _ _[*e.g., 3*]_ _ calendar years and all budgets prepared in relation to the current year and the prior _ _[*e.g., 3*]_ _ years. Copies of all invoices, utility bills, and other records of operating expenses incurred during the current years and the prior _ _[*e.g., 3*]_ _ years must be made available for inspection by Buyer at reasonable times at _ _[*address*]_ _.

3.1.12. Loan Documents Related to Assumed Loan. Copies of all notes, deeds of trust, loan agreements, applications, guaranties, other securities documents, and any correspondence related to the Assumed Loan.

3.1.13. Insurance Policies. Copies of all liability, fire, and casualty insurance policies carried by Seller, and copies of certificates evidencing all insurance that tenants of the Property are required to carry.

3.1.14. Materials Related to Condition of the Property. Any environmental impact reports, "Phase I" or "Phase II" reports, or environmental site assessments concerning hazardous materials on the Property, complaints or notices of the presence of hazardous materials on the Property, geological surveys, soil tests, engineering reports, inspection results, complaints, or notices received regarding the safety of the Property.

3.1.15. Litigation Materials. All materials related to pending or threatened litigation, or litigation that was pending or threatened during the period of Seller's ownership of the Property, involving the Property or the Seller on account of its ownership of the Property, including correspondence, complaints, court orders, settlements, and judgments.

3.1.16. Other Documents. All other data, correspondence, documents, agreements, waivers, notices, applications, and other records regarding the Property relating to transactions with taxing authorities, governmental agencies, utilities, vendors, tenants, neighbors, and others with whom Buyer may be dealing from and after the Closing Date.

3.1.17. Excluded Records. The Preliminary Documents will not include any books, records, documents, or information on the corporate, financial, and accounting records of the operations of Seller as an entity (as opposed to records concerning the Property), regarding offers or inquiries made by third parties concerning the purchase of some or all of the Property or appraisals of the value of the Real Property that are attorney-client communications of Seller, that are Seller's attorney's work product, or that are not in the possession of Seller or persons under Seller's control.

4.171-2 Buyer's approval of preliminary documents

[*Add one of the following alternatives*]

[*Alternative 1: Buyer's form of approval of preliminary documents*]

3.2. Buyer's Approval of Preliminary Documents. Buyer's obligation to purchase the Property is expressly conditioned on its approval, in its sole discretion, of the matters disclosed in the Preliminary Documents. Buyer will have the period from the Effective Date until the date that is _ _[*number*]_ _ days after delivery to Buyer of the last Preliminary Document (Contingency Date) to review the Preliminary Documents and to decide whether to approve the matters disclosed in the Preliminary Documents. On or before the Contingency Date, Buyer will

deliver written notice to Seller either accepting the matters disclosed in the Preliminary Documents or terminating this Agreement. If Buyer fails to give such notice on or before the Contingency Date, Buyer will be deemed to have elected to terminate this Agreement.

[*Alternative 2: Seller's form of approval of preliminary documents*]

3.2. Buyer's Approval of Preliminary Documents. Buyer's obligation to purchase the Property is expressly conditioned on its approval, in its sole discretion, of the matters disclosed in the Preliminary Documents. Buyer will have the period from the Effective Date until the date that is _ _[*number*]_ _ days after the Effective Date (Contingency Date) to review the Preliminary Documents and to decide whether to approve the matters disclosed in the Preliminary Documents. On or before the Contingency Date, Buyer must deliver written notice to Seller either accepting the matters disclosed in the Preliminary Documents or terminating this Agreement. If Buyer fails to give such notice on or before the Contingency Date, Buyer will be deemed to have accepted the matters disclosed in the Preliminary Documents. By its acceptance or waiver of the contingencies set forth in this _ _[*e.g., section 3.2*]_ _, Buyer will be deemed to have acknowledged that (a) Seller has provided Buyer with access to the Preliminary Documents and (b) Buyer has had ample opportunity to review and inspect the Preliminary Documents and to make such independent factual, physical, and legal examinations and inquiries as Buyer deems necessary or desirable with respect to matters disclosed in the Preliminary Documents.

[*Continue*]

4.171-3 Buyer's approval of contracts

3.3. Buyer's Approval of Contracts. Buyer's obligation to purchase the Property is expressly conditioned on its approval, in its sole discretion, of all service contracts, management agreements, maintenance contracts, and other contracts and agreements related to or affecting the operation of the Property and not included as part of the title documents (collectively, the Contracts). Buyer shall have until the date that is _ _[*e.g., 10*]_ _ business days before the Contingency Date to either approve or disapprove any Contracts (Disapproved Contracts). Seller shall have until _ _[*e.g., 5*]_ _ business days before the Contingency Date to notify Buyer, in writing, of its agreement to terminate the Disapproved Contracts on or before the Closing Date. In no event, however, shall Seller be required to terminate any Contracts that by their terms are not terminable before the Closing unless Buyer agrees, in writing, to pay at Closing any prorated charges or other costs associated with such early termination. Failure by Seller to agree to terminate the Disapproved Contracts within the specified period shall be deemed Seller's election not to terminate the Disapproved Contracts. On or before the Contingency Date, Buyer shall deliver written notice to Seller either accepting the Disapproved Contracts that Seller elected (or is deemed to have elected) not to terminate or terminating this Agreement.

4.171-4 Approval of title

3.4. Approval of Title. Buyer's obligation to purchase the Property is expressly conditioned on Buyer's approval of the condition of title of the Property in accordance with the following procedure:

3.4.1. Permitted Exceptions. The following exceptions shown on the Preliminary Report (Permitted Exceptions) are approved by Buyer: (a) exceptions for a lien for local real estate taxes and assessments not yet due or payable,

[*Add if appropriate*]

including (without limitation) special taxes under Govt C §§53311-53368.3 or installment assessments under Street & H C §§8500-8887,

[*Continue*]

(b) the standard preprinted exceptions and exclusions of the Title Company, (c) the lien arising from the Assumed Loan, (d) any other exception shown on the Preliminary Report, other than exceptions for monetary liens (excluding the lien arising from the Assumed Loan), which Buyer does not object to by written notice to Seller within _ _[*e.g., 10*]_ _ days after delivery of the Preliminary Report (Buyer's Title Notice), or as otherwise provided in this _ _[*e.g., section 3.4*]_ _. All exceptions on the Preliminary Report other than the Permitted Exceptions will be Title Objections. If Buyer fails to deliver Buyer's Title Notice within the time specified in this _ _[*e.g., section 3.4*]_ _, Buyer will be deemed to have objected to each title exception shown in the Preliminary Report that is not otherwise a Permitted Exception.

3.4.2. Title Objections. With respect to any Title Objection arising or resulting from any act or omission of Seller, Seller will have _ _[*e.g., 10*]_ _ days after delivery of Buyer's Title Notice (or Buyer's deemed objection to all exceptions) to specify the manner in which it will remove or cure such Title Objection. With respect to any Title Objection that did not arise or result from any act or omission of Seller, Seller will have _ _[*e.g., 10*]_ _ days after delivery of Buyer's Title Notice to give notice to Buyer in writing (Seller's Title Notice), stating either (a) the manner in which Seller will remove or cure such Title Objection, or (b) that Seller will not remove or cure such Title Objection. If Seller fails to deliver Seller's Title Notice within the time specified in this _ _[*e.g., section 3.4*]_ _, Seller will be deemed to have elected not to cure such Title Objection. Despite the foregoing, Seller agrees to remove all liens securing the payment of money that encumber the Property, other than the lien arising from the Assumed Loan.

3.4.3. Seller Elects Not to Cure. If Seller elects not to cure or remove a Title Objection (or is deemed to have so elected), then Buyer will have _ _[*e.g., 10*]_ _ days after delivery of the Seller's Title Notice to deliver a written notice to Seller (Buyer's Election Notice) of Buyer's election either to (a) proceed with the purchase of the Property, waive such Title Objection, and accept the exception shown in the Preliminary Report as a Permitted Exception, or (b) terminate this Agreement. If Buyer fails to deliver Buyer's Election Notice within the time specified in this _ _[*e.g., section 3.4*]_ _, Buyer will be deemed to have elected to terminate this Agreement.

3.4.4. Nonmonetary Cure. If Seller is obligated or elects to cure or remove a Title Objection, but the method specified for removing or curing the Title Objection is other than the payment of a specific sum of money, then Buyer will have _ _[*e.g., 10*]_ _ days after delivery of the Seller's Title Notice to deliver Buyer's Election Notice specifying whether it elects to (a) proceed with the purchase of the Property, subject to Seller's removal of the Title Objection, or (b) terminate this Agreement. If Buyer fails to deliver Buyer's Election Notice within the time specified in this _ _[*e.g., section 3.4*]_ _, Buyer will be deemed to have elected to terminate this Agreement.

3.4.5. Additional Encumbrances. If any encumbrance or other exception to title arises or is discovered after the delivery of the Preliminary Report (Additional Encumbrance), the party discovering such Additional Encumbrance must promptly give written notice to the other. No later than _ _[*e.g., 5*]_ _ days after delivery of the notice of such Additional Encumbrance, Buyer will deliver a new Buyer's Title Notice to Seller specifying whether the Additional Encumbrance is a Title Objection or a Permitted Exception. If Buyer objects to the Additional Encumbrance, the parties will proceed in the same manner as set forth above for Title Objections arising from the Preliminary Report. If Buyer fails to deliver Buyer's Election Notice within the time specified in this _ _[*e.g., section 3.4*]_ _, Buyer will be deemed to have elected to terminate this Agreement.

3.4.6. Seller's Failure to Remove Title Objection. If Seller is obligated or elects to cure or remove a Title Objection and fails to do so least _ _[*e.g., 5*]_ _ days before the Closing Date, or fails to show that it will be able to do so on Closing, then Seller will be in default under this Agreement, and Buyer will have all its rights and remedies provided by this Agreement.

4.171-5 Review of preliminary documents and physical condition

3.5. Review of Preliminary Documents and Physical Condition.

3.5.1. Due Diligence. Buyer's obligation to purchase the Property is expressly conditioned on its approval, in its sole discretion, of the condition of the Property and all other matters concerning the Property, including without limitation economic, financial, and accounting matters relating to or affecting the Property or its value, and the physical and environmental condition of the Property. Buyer will have until the Contingency Date to conduct such investigations as Buyer may choose (Due Diligence) to determine, in its sole discretion, whether this contingency is met. On or before the Contingency Date, Buyer will deliver written notice to Seller accepting the Property, or terminating this Agreement. If Buyer fails to give such notice on or before the Contingency Date, Buyer will be deemed to have elected to terminate this Agreement.

3.5.2. Access to Property. As part of its Due Diligence, Buyer may investigate economic, financial, and accounting matters relating to or affecting the Property or its value, and conduct inspections, tests, and studies with respect to the physical and environmental condition of the Property. Buyer and Buyer's consultants, agents, engineers, inspectors, contractors, and employees (Buyer's Representatives) must be given reasonable access to the Property during regular business hours for the purpose of performing such Due Diligence. Buyer will undertake the Due Diligence at its sole cost and expense, except as provided in _ _[*e.g., section 9.2*]_ _.

Buyer will indemnify, defend with counsel reasonably acceptable to Seller, and hold Seller harmless from all claims (including claims of lien for work or labor performed or materials or supplies furnished), demands, liabilities, losses, damages, costs, fees, and expenses, including Seller's reasonable attorney fees, costs, and expenses, arising from the acts or activities of Buyer or Buyer's Representatives in, on, or about the Property during or arising in connection with Buyer's inspections of the Property.

[*If applicable, add the following option*]

[*Option: Seller's clause requiring buyer to assume risk*]

3.5.3. Assumption of Risk. Subject to the other provisions of this Agreement, Buyer agrees that, by its acceptance or waiver of the contingency in this _ _[*e.g., section 3.5*]_ _, it assumes the risk that an adverse condition of the Property may not have been revealed by its own Due Diligence. On Buyer's acceptance or waiver of the contingency in this _ _[*e.g., section 3.5*]_ _, Seller will have no obligation to repair, correct, or compensate Buyer for any condition of the Property, including defects in the Improvements, noncompliance with applicable laws and regulations, including without limitation zoning laws, building codes, and the Americans with Disabilities Act, whether or not such condition of the Property would have been disclosed by Buyer's Due Diligence.

[*Continue*]

4.171-6 Financing contingency

3.6. Financing Contingency. Buyer's obligation to purchase the Property is conditioned on Buyer's obtaining, before the Contingency Date, a written commitment for a loan from _ _[*name of lender*]_ _ of at least _ _[*amount*]_ _ Dollars (_ _[*dollar amount*]_ _), secured by a first priority deed of trust on the Property on terms no less favorable than interest at _ _[*number*]_ _ percent (_ _[*number*]_ _%) per year, for a term of _ _[*number*]_ _ (_ _[*number*]_ _) years, amortized over _ _[*number*]_ _ (_ _[*number*]_ _) years, with loan fees not to exceed _ _[*e.g., one*]_ _ percent (_ _[*e.g., 1%*]_ _) of the principal amount of the loan, with prepayment permitted at the option of the Buyer subject to a prepayment penalty not to exceed _ _[*e.g., one*]_ _ percent (_ _[*e.g., 1%*]_ _) of the then-outstanding principal amount of the loan, and with such other terms and conditions as Buyer may approve in its sole and absolute discretion. Buyer agrees to use commercially reasonable efforts to obtain such a loan commitment. On or before the Contingency Date, Buyer must deliver written notice to Seller indicating whether the contingency set forth in this _ _[*e.g., section 3.6*]_ _ (Financing Contingency) has been met and waiving the Financing Contingency or terminating this Agreement unless Seller elects to provide such financing. If Buyer fails to deliver such notice on or before the Contingency Date, then Buyer will be deemed to have elected to terminate this Agreement unless the Seller elects to provide such financing. If the Financing Contingency is not met or waived by the Contingency Date, Seller may, but is not obligated to, agree to provide such financing on the terms listed above and in accordance with the note and deed of trust attached to this Agreement as _ _[*e.g., Exhibits B and C*]_ _. If Seller delivers a written commitment to Buyer within _ _[*e.g., 3*]_ _ business days after the Contingency Date, the Financing Contingency will be deemed met.

3.7. Termination for Failure of a Contingency. If this Agreement is terminated or deemed to be terminated for failure of a contingency set forth in this _ _[*e.g., Article 3*]_ _, then immediately on written notice from Buyer, Escrow Holder must refund the Deposit and return any Letter of Credit to Buyer, without offset for any charges or claims. Any cancellation fee or other costs of the Escrow Holder or the Title Company resulting from this termination for failure of a contingency will be borne equally by Seller and Buyer, and each party must pay its own expenses.

Comment: On buyer's due diligence, see §§4.45-4.100. For additional provisions to add to section 3.5 on the financing contingency, see forms 9.38-1, 9.45-1, 9.97-1—9.102-1.

© The Regents of the University of California

§4.172 F. Form: Seller's Preclosing Covenants

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§4.166-4.182.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

4.172-1 No amendments or agreements

ARTICLE 4

SELLER'S PRECLOSING COVENANTS

4.1. No Amendments or Agreements. On or after the Effective Date, Seller will not (a) amend or waive any right under any Preliminary Document or (b) enter into any lease or other agreement of any type affecting the Property that would survive the Closing Date, without Buyer's prior written consent. Before the Contingency Date, Buyer may not unreasonably withhold its consent under this _ _[*e.g., section 4.1*]_ _; after the Contingency Date, however, Buyer will have sole discretion in all such matters.

4.172-2 Insurance

4.2. Insurance. Through the Closing Date, Seller must maintain or cause to be maintained in full force and effect comprehensive general liability casualty and other insurance on the Property in an amount equal to the full replacement cost of the Improvements.

4.172-3 Maintenance and operation

4.3. Maintenance and Operation. Seller, at its sole cost and expense, must operate the Property in substantially the same manner as it has operated the Property before the Effective Date and must maintain and keep the Property such that on the Closing Date the Property is in at least as good condition and repair as on the Effective Date, reasonable wear and tear excepted. Seller may not make any material alterations to the Property without Buyer's prior written consent.

4.172-4 Mechanics' liens

4.4. Mechanics' Liens. Except for materials, supplies, or work provided or ordered for the Property at the request of or for the account of Buyer, on or before the Closing, Seller must (a) pay for all materials, supplies, and work provided or ordered for the Property for which a labor, materialman's, or mechanics' lien may be claimed under applicable law and (b) if required by the Title Company, provide the Title Company with such indemnifications or security as it may require to insure title to the Property at the Closing without exception for any unrecorded labor, materialmen's, or mechanics' claim of lien.

4.172-5 No marketing

4.5. No Marketing. Seller agrees not to market, show, or list the Property to any other prospective buyer during the term of this Agreement.

4.172-6 Existing financing

4.6. Existing Financing. Seller must not permit any default, or any event that could give rise to a default with lapse of time or notice, to occur under any existing loan secured by the Property or other financing encumbering the Property.

4.172-7 Licenses and permits

4.7. Licenses and Permits. Seller will use due diligence and its best efforts to keep in full force and effect, and will renew when necessary, all licenses and permits for the Property.

4.172-8 Access to property

4.8. Access to Property. Buyer and Buyer's representatives, agents, and designees will have the right at all reasonable times until Closing to enter the Property as provided in _ _[*e.g., section 3.5.2*]_ _.

4.172-9 Notification

4.9. Notification. Seller will promptly notify Buyer of any material change in any condition with respect to the Property or of any material event or circumstance that makes any representation or warranty of Seller under this Agreement untrue or misleading.

4.172-10 Estoppel certificates

4.10. Estoppel Certificates. Seller agrees to use its best efforts to obtain the estoppel certificates described in _ _[*e.g., section 6.1.4*]_ _.

4.172-11 Service contracts

4.11. Service Contracts. Seller covenants and agrees that before the Closing Date it will terminate all service contracts related to the Property except any that Buyer has specifically elected to assume under _ _[*e.g., section 3.3*]_ _.

Comment: On seller's preclosing covenants, see §§4.101-4.106.

© The Regents of the University of California

§4.173 G. Form: Representations and Warranties

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§4.166-4.182.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

4.173-1 Representations and warranties

ARTICLE 5

REPRESENTATIONS AND WARRANTIES

[*Add one of the following alternatives*]

[*Alternative 1: Buyer's form of seller's representations and warranties*]

5.1. Seller's Representations and Warranties. Seller hereby represents and warrants that each of the following is true as of the Effective Date and the Closing Date:

5.1.1. Condition of the Property. The Property is free of any physical or mechanical defects and all building systems in the Improvements (including without limitation heating, ventilating, air-conditioning, elevator, other mechanical, electrical, sprinkler, life safety, and plumbing systems) are in good order and repair.

5.1.2. Compliance With Laws. Neither the Property nor its operation violates in any way any applicable laws, ordinances, rules, regulations, judgments, orders, or covenants, conditions and restrictions, whether federal, state, local, foreign, or private, including without limitation the Americans with Disabilities Act and all life safety requirements. The Improvements are not in violation of any applicable building or zoning codes, building moratorium or environmental protection codes, laws, regulations, or ordinances. Seller has not received any request, oral or written, that Seller modify or terminate any use of the Property. The zoning of the Property permits the current Improvements and use of the Property, there is no pending or contemplated rezoning, and the Property complies with the Subdivision Map Act and local ordinances enacted under that Act.

5.1.3. Documents. All Preliminary Documents delivered to Buyer under _ _[*e.g., section 3.1*]_ _, and all other documents delivered to Buyer by or on behalf of Seller, are true, correct, and complete copies of what they purport to be. The documents delivered by Seller to Buyer are all the material documents concerning the Property in Seller's possession or under its control.

5.1.4. Leases. The Rent Roll and Updated Rent Roll (defined in _ _[*e.g., section 6.1.4*]_ _) are true, correct, and complete. Seller has delivered to Buyer true, accurate, and complete copies of all Leases, and there are no leases, subleases, occupancies, or tenancies in effect pertaining to the Property except as stated in the Leases. The Leases are in full force and effect; no party to the Leases is in default under the Leases; and the Leases are subject to no defenses, setoffs, or counterclaims for the benefit of the tenants under the Leases; and no rent has been prepaid nor concessions given to the tenants under the Leases except as disclosed in the Leases. Seller has no notice or knowledge that any tenant of the Property is the subject of a bankruptcy or insolvency proceeding. Seller may not modify, cancel, amend, or extend any Lease or waive any rights under the Leases or enter into any new tenant lease between the Effective Date and the Closing Date without Buyer's prior written approval, which approval must not be unreasonably withheld. Seller is in full compliance with all of the landlord's obligations under the Leases.

5.1.5. Operating Statements. All operating statements furnished to Buyer in connection with or under this Agreement (a) are true and correct in all material respects, (b) have been prepared in conformity with generally accepted accounting principles consistently applied, and (c) accurately reflect the financial position of the Property.

5.1.6. Litigation. There is no pending or threatened private or governmental litigation by any

governmental authority or person against Seller relating to the Property that might, if it and all other pending and threatened litigation were adversely determined, result in a material adverse change in the Property or its operation or that challenges the validity of or otherwise materially adversely affects the transactions contemplated by this Agreement.

5.1.7. Other Proceedings. No attachments, execution proceedings, assignments for the benefit of creditors, insolvency, bankruptcy, reorganization, or other proceedings are pending or threatened against Seller or Seller's interest in the Property, nor are any such proceedings contemplated by Seller.

5.1.8. Governmental Action. Seller has no knowledge of, nor has Seller received written notice of, any plan, study, or effort by any agency or party that in any way would materially affect the use of the Property or any portion of it for its current use, or of any intended public improvements that would result in any charge being levied against, or any lien assessed on, the Property. Seller has no knowledge of any existing, proposed, or contemplated plan to widen, modify, or realign any street or highway contiguous to the Property.

5.1.9. Condemnation. Seller has received no notice of any currently pending or contemplated special assessments or proceedings to condemn or demolish the Property or any part of it or any proceedings to declare the Property or any part of it a nuisance.

5.1.10. Utilities. All water, sewer, gas, electric, telephone, drainage facilities, and all other utilities required by law or by the normal operation of the Property are adequate to service the Property in its present use and to permit full compliance with all requirements of law and normal usage by the tenants of the Property.

5.1.11. Licenses. Seller has all licenses, permits, easements, and rights of way, including proof of dedication, building permits, and occupancy permits that are required from any governmental authority having jurisdiction over the Property, or from private parties, in order to continue the present use of the Property and to ensure adequate vehicular and pedestrian access to the Property. Such licenses, permits, easements, and rights-of-way must be in full force and effect on the Closing Date. All permits, rights, and documents to be transferred to Buyer at close of escrow have been fully paid for and are not subject to any liens, encumbrances, or claims of any kind, and their transfer and assignment do not require the consent of third parties other than as set forth in such documents or as required by law. Seller has, and at close of escrow will deliver to Buyer, good and marketable title to all such permits, rights, and documents.

5.1.12. Development Rights. Neither Seller nor any previous owner of the Property has, except by operation of law, sold, transferred, conveyed, or entered into any agreement regarding "air rights," "excess floor area ratio," or other development rights or restrictions relating to the Property, except as otherwise expressly set forth in the Preliminary Report.

5.1.13. Due Authorization. This Agreement and the performance of Seller's obligations under it and all documents executed by Seller that are to be delivered to Buyer at the Closing are, or on the Closing Date will be, duly authorized, executed, and delivered by Seller and are, or at the Closing Date will be, legal, valid, and binding obligations of Seller, and do not, and on the Closing Date will not, violate any provision of any agreement or judicial order to which Seller is a party or to which Seller or the Property is subject. No consent of any partner, shareholder, creditor, investor, judicial or administrative body, government agency, or other party is required for Seller to enter into and/or to perform Seller's obligations under this Agreement, except as has already been obtained. Seller is a corporation organized, validly existing, and in good standing under the laws of the State of _ _[*name*]_ _[.]

[*If not a California corporation, add*]

and is qualified to do business in the State of California.

[*Continue*]

5.1.14. Title to the Property. Seller has good and marketable title to the Property. Seller has no actual knowledge of any unrecorded or undisclosed legal or equitable interest in the Property owned or claimed by anyone other than Seller. Seller has no knowledge that anyone will, at the Closing, have any right to possession of the Property, except as disclosed by this Agreement or otherwise in writing to Buyer. There are no unsatisfied mechanics' or materialmen's lien rights on the Property. No assessment lien or bond encumbers the Property, and no governmental authority has undertaken any action that could give rise to an assessment

lien affecting the Property.

5.1.15. Personal Property. Seller has no knowledge that anyone will, at the Closing, have any right to possession of any personal property included in the Purchase Price nor knowledge of any liens or encumbrances affecting such personal property, except as disclosed by this Agreement or otherwise in writing to Buyer.

5.1.16. Hazardous Wastes. The Property is not in violation of any federal, state, or local law, ordinance, or regulation relating to industrial hygiene or to the environmental conditions on, under, or about the Property, including but not limited to soil and groundwater conditions. There are no environmental, health, or safety hazards on, under, or about the Property, including but not limited to soil and groundwater conditions. Neither Seller nor any third party (including but not limited to Seller's predecessors in title to the Property) has used or installed any underground tank, or used, generated, manufactured, treated, stored, placed, deposited, or disposed of on, under, or about the Property or transported to or from the Property any flammable explosives, radioactive materials, hazardous wastes, toxic substances, or related materials (Hazardous Materials), which for purposes of this Agreement include, but are not limited to, substances defined as "hazardous substances, hazardous materials, or toxic substances" in the Comprehensive Environmental Response, Compensation and Liability Act of 1980, as amended (42 United States Code §§9601 et seq.); the Hazardous Materials Transportation Safety and Security Reauthorization Act (49 United States Code §§5101 et seq.); the Resource Conservation and Recovery Act (42 United States Code §§6901 et seq.); the substances defined as "hazardous wastes" in California Health and Safety Code §25117 or as "hazardous substances" in California Health and Safety Code §25316; and the chemicals known to cause cancer or reproductive toxicity as published in the Safe Drinking Water and Toxic Enforcement Act of 1986 (California Health and Safety Code §25249.5 et seq.); and in the regulations adopted and publications promulgated under each of the aforesaid laws). Seller has no actual knowledge, except as otherwise disclosed to Buyer in writing, of the existence or prior existence on the Property of any Hazardous Material, other than de minimis amounts of household cleaners or office supplies.

5.1.17. Foreign Person. Seller is not a foreign person and is a "United States Person" as such term is defined in §7701(a)(30) of the Internal Revenue Code of 1986, as amended.

[*Alternative 2: Seller's form of seller's representations and warranties*]

5.1. Seller's Representations and Warranties. Despite anything to the contrary in this Agreement, Seller warrants and represents as of the Effective Date that:

5.1.1. Organization; Authority. This Agreement and the performance of Seller's obligations under it and all documents executed by Seller that are to be delivered to Buyer at the Closing are, or on the Closing Date will be, duly authorized, executed, and delivered by Seller and are, or at the Closing Date will be, legal, valid, and binding obligations of Seller, and do not, and on the Closing Date will not, violate any provision of any agreement or judicial order to which Seller is a party or to which Seller or the Property is subject. No consent of any partner, shareholder, creditor, investor, judicial or administrative body, government agency, or other party is required for Seller to enter into or to perform Seller's obligations under this Agreement, except as has already been obtained. Seller is a corporation organized, validly existing, and in good standing under the laws of the State of _ _[*name*]_ _[.]

[*If not a California corporation, add*]

and is qualified to do business in the State of California.

[*Continue*]

5.1.2. No Violation of Law. To Seller's knowledge, Seller has received no written notice of any currently outstanding violations of any federal, state, county, or municipal law, ordinance, order, regulation, or requirement affecting the Property.

5.1.3. Litigation. To Seller's knowledge, Seller has not received any written notice of any existing or threatened litigation or arbitration involving the Property.

5.1.4. Preliminary Documents. To Seller's knowledge, the Preliminary Documents constitute all books, records, documents, agreements, contracts, reports, and other materials related to the Property that are in Seller's possession or control. To Seller's knowledge, the Preliminary Documents are true, correct, and

complete copies of what they purport to be.

5.1.5. No Condemnation. To Seller's knowledge, Seller has received no written notice of any presently pending or contemplated special assessments or proceedings to condemn or demolish the Property or any part of it, or any proceedings to declare the Property or any part of it a nuisance.

5.1.6. Hazardous Wastes. To Seller's knowledge, Seller has received no written notice of any Hazardous Materials located on, under, or about the Property, except as disclosed in the Preliminary Documents.

5.1.7. Foreign Person. Seller is not a foreign person and is a "United States Person" as that term is defined in §7701(a)(30) of the Internal Revenue Code of 1986, as amended.

5.1.8. Seller's Knowledge. As used in this Agreement, the phrase "Seller's knowledge" will be limited to the actual knowledge of _ _[*name(s) of individual(s)*]_ _, without duty of inquiry or investigation into the matter so qualified. "Seller's knowledge" will not be construed to refer to the knowledge of any other agent or employee or principal of Seller. _ _[*Name(s) of individual(s)*]_ _ _ _[*is/are*]_ _ the employee(s) of Seller with the primary responsibility for the matters that are the subject of these representations and warranties. _ _[*Name(s) of individual(s)*]_ _ will have no personal liability to Buyer for any breach of any representation or warranty in this Agreement.

[*Continue*]

4.173-2 Buyer's representations and warranties

5.2. Buyer's Representations and Warranties. Despite anything to the contrary in this Agreement, Buyer hereby warrants and represents that each of the following is true as of the Effective Date and the Closing Date:

5.2.1. Due Authorization. This Agreement and the performance of Buyer's obligations under it and all the documents executed by Buyer that are to be delivered to Seller at the Closing are, or on the Closing Date will be, duly authorized, executed, and delivered by Buyer and are, or at the Closing Date will be, legal, valid, and binding obligations of Buyer, and do not, and on the Closing Date will not, violate any provisions of any agreement or judicial order to which Buyer is a party or to which Buyer or the Property is subject. No consent of any partner, shareholder, creditor, investor, judicial or administrative body, government agency, or other party is required for Buyer to enter into or to perform Buyer's obligations under this Agreement, except as has already been obtained. Buyer is a corporation organized, validly existing, and in good standing under the laws of the State of _ _[*name*]_ _[.]

[*If not a California corporation, add*]

and is qualified to do business in the State of California.

5.2.2. USA Patriot Act Representation. _ _[*To Buyer's actual knowledge:*]_ _

5.2.2.1. Neither Buyer nor its partners, members, officers, directors, investors, or shareholders, nor any of their respective affiliates, is in violation of any federal or state anti-money laundering and anti-terrorism laws[.]

[*If appropriate, add*]

provided that the preceding representation shall not apply to Buyer's shareholders if Buyer is a publicly traded company.

[*Continue*]

5.2.2.2 Neither Buyer nor its partners, members, officers, directors, investors, or shareholders, nor any of their respective affiliates, is acting, directly or indirectly, on behalf of terrorists, terrorist organizations, or narcotics traffickers, including those persons or entities designated as a Specially Designated National pursuant to Executive Order 13224 of the President of the United States, dated September 23, 2001 (Executive Order), as amended, or that appear on the Annex to the Executive Order, or are included on any relevant lists maintained by the Office of Foreign Assets Control of U.S. Department of Treasury, U.S. Department of State, or other U.S. government agencies, all as may be amended from time to time (Government List)[.]

[*If appropriate, add*]

provided that the preceding representation shall not apply to Buyer's shareholders if Buyer is a publicly traded company.

[*Continue*]

5.2.2.3. Neither Buyer nor its partners, members, officers, directors, investors, or shareholders, nor any of their respective affiliates, in any capacity in connection with the purchase of Property (a) conducts any business or engages in making or receiving any contribution of funds, goods, or services to or for the benefit of any person included in a Government List, (b) deals in, or otherwise engages in any transaction relating to, the Property or interests in property blocked pursuant to the Executive Order, or (c) engages in or conspires to engage in any transaction that evades or avoids, or has the purpose of evading or avoiding, or attempts to violate, any of the prohibitions set forth in any anti-money-laundering and anti-terrorism laws[.]

[*If appropriate, add*]

provided that the preceding representation shall not apply to Buyer's shareholders if Buyer is a publicly traded company.

[*Continue*]

5.2.2.4. Neither Buyer, nor any person controlling or controlled by Buyer, is a country, territory, individual, or entity named on a Government List, and, to Buyer's actual knowledge, the monies used in connection with this Agreement and amounts committed with respect to this Agreement were not and are not derived from any activities that contravene any applicable anti-money-laundering or anti-bribery laws and regulations (including funds being derived from any person, entity, country, or territory on a Government List or engaged in any unlawful activity defined under 18 USC §1956(c)(7)).

4.173-3 Effect of representations and warranties

5.3. Effect of Representations and Warranties. Each representation and warranty in this _ _[*e.g., Article 5*]**_ _ (a) is material and being relied on by the party to which the representation and warranty is made; (b) is true in all respects as of the Effective Date; (c) must be true in all respects on the Closing Date; and (d) will survive the Closing, except as otherwise provided in this Agreement.**

[*Continue*]

[*If seller's form of representations and warranties, add sections 5.4-5.6 (form 4.173-4—4.173-6)*]

4.173-4 Survival of representations and warranties and limitation on liability

5.4. Survival of Seller's Representations and Warranties and Limitation on Liability. The parties agree that (a) Seller's warranties and representations in this Agreement and in any document (including any estoppel or other certificate) executed by Seller under this Agreement with respect to the Property will survive for _ _[*e.g., 6*]**_ _ months after the Closing Date, and (b) if Buyer fails to provide written notice to Seller of any breach of such warranties or representations within _ _**[*e.g., 6*]**_ _ after the Closing Date, Buyer will be deemed to have waived all claims for breach of any representations and warranties with respect to the Property. Buyer's sole remedy will be an action at law for damages as a consequence of such breach or termination of this Agreement under _ _**[*e.g., section 9.4*]**_ _ and waiver of any further claims against Seller. In no event will Seller's liability for damages to Buyer after the Closing exceed _ _**[*dollar amount*]**_ _.**

4.173-5 "As is" purchase

5.5. "As Is" Purchase. Subject to the approval or waiver of the Contingencies in _ _[*e.g., Article 3*]**_ _, Seller's preclosing obligations under _ _**[*e.g., Article 4*]**_ _, the closing conditions in _ _**[*e.g., Article 6*]**_ _, and as a material inducement to Seller's execution and delivery of this Agreement and performance of its duties under this Agreement: EXCEPT AS OTHERWISE PROVIDED IN THIS AGREEMENT, BUYER HAS AGREED TO ACCEPT POSSESSION OF THE PROPERTY ON THE CLOSING DATE ON AN "AS IS" BASIS. SELLER AND BUYER AGREE THAT THE PROPERTY WILL BE SOLD "AS IS, WHERE IS, WITH ALL FAULTS" WITH NO RIGHT OF SET-OFF OR REDUCTION IN THE PURCHASE PRICE, AND, EXCEPT AS SET FORTH IN _ _**[*e.g., section 5.1*]**_ _ OF THIS AGREEMENT, SUCH SALE WILL BE WITHOUT REPRESENTATION OR WARRANTY OF ANY KIND, EXPRESS OR IMPLIED (INCLUDING, WITHOUT LIMITATION, WARRANTY OF INCOME POTENTIAL, OPERATING EXPENSES, USES, MERCHANTABILITY, OR FITNESS FOR A PARTICULAR PURPOSE), AND SELLER**

DISCLAIMS AND RENOUNCES ANY SUCH REPRESENTATION OR WARRANTY.

4.173-6 Release

5.6. Release. Except as provided in _ _[*e.g., section 5.4*]_ _, effective from and after the Closing, Buyer hereby waives, releases, acquits, and forever discharges Seller, and Seller's agents, directors, officers, and employees to the maximum extent permitted by law, of and from any and all claims, actions, causes of action, demands, rights, liabilities, damages, losses, costs, expenses, or compensation whatsoever, direct or indirect, known or unknown, foreseen or unforeseen, that it now has or that may arise in the future because of or in any way growing out of or connected with this Agreement and the Property (including without limitation the Condition of the Property), except matters arising from Seller's fraud or intentional misrepresentation. BUYER EXPRESSLY WAIVES ITS RIGHTS GRANTED UNDER CALIFORNIA CIVIL CODE §1542, AND ANY OTHER PROVISION OF LAW THAT PROVIDES A GENERAL RELEASE DOES NOT EXTEND TO CLAIMS THAT BUYER DOES NOT KNOW OR SUSPECT TO EXIST IN ITS FAVOR AT THE TIME OF EXECUTING THE RELEASE, WHICH IF KNOWN BY IT MUST HAVE MATERIALLY AFFECTED ITS AGREEMENT TO RELEASE SELLER.

Seller and Buyer have each initialed this _ _[*e.g., section 5.6*]_ _ to further indicate their awareness and acceptance of each and every provision of this Agreement. The provisions of this _ _[*e.g., section 5.6*]_ _ will survive the Closing.

Seller's Initials: _____

Buyer's Initials: _____

Comment: On seller's representations and warranties, see §§4.107-4.120; on releases, see §4.125. See also discussion of due diligence in §§4.45-4.100. For alternative provisions on representations regarding hazardous substances, see §§7.29-7.33.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.174 H. Form: Closing Conditions

§4.174 H. Form: Closing Conditions

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§4.166-4.182.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

4.174-1 Buyer's closing conditions

ARTICLE 6

CLOSING CONDITIONS

6.1. Buyer's Closing Conditions. All obligations of Buyer under this Agreement are subject to the fulfillment, before or at the Closing, of each of the following conditions (Buyer's Closing Conditions). Buyer's Closing Conditions are solely for Buyer's benefit and any or all of Buyer's Closing Conditions may be waived in writing by Buyer in whole or in part without prior notice.

6.1.1. Title. It is a Buyer's Closing Condition that, on the Closing Date, Seller convey to Buyer marketable fee simple title to the Real Property by execution and delivery of a grant deed in the form attached to this Agreement as _ _[*e.g., Exhibit D*]_ _ (Deed) and cause to be delivered to Buyer from the Title Company an ALTA (_ _[*B-1970 Form, as amended/June 1, 1987, Form*]_ _) Owner's Extended Coverage Policy of Title Insurance with liability in the full amount of the Purchase Price, insuring title to the Real Property in Buyer, subject only to the Permitted Exceptions, together with such endorsements described below or as may be reasonably requested by Buyer (Title Policy). The Title Policy must also include such endorsements or guaranties as Buyer may request. Seller must deliver to the Title Company such instruments, documents, releases, and agreements and must perform such other acts as Title Company may reasonably require in order to issue the Title Policy. Indemnification of the Title Company to induce it to insure any otherwise unpermitted exception to title will not be allowed except with Buyer's prior written consent after full disclosure to Buyer of the nature and substance of such exception and indemnity, which consent will not be unreasonably withheld by Buyer for exceptions not material to marketable title to the Real Property.

6.1.2. Liens. Buyer must have received a certified report, with copies of all documents, satisfactory to Buyer and Buyer's counsel, from the Title Company or a reputable lien search company indicating that there are no personal property liens of record on file with the Secretary of State of California, other than those that will be discharged at the Closing, as of a date no more than _ _[*e.g., 10*]_ _ business days before the Closing Date, and a confirmation dated no more than _ _[*e.g., 3*]_ _ business days before the Closing Date that no further liens have been filed since the date of the certified report. Also, Buyer must have received a verified report, satisfactory to Buyer and Buyer's counsel, from the Title Company or a reputable lien search company, indicating that there are no federal or state tax liens of record against the Property and on file with the respective agencies as of a date no more than _ _[*e.g., 10*]_ _ business days before the Closing Date.

6.1.3. Seller's Representations, Warranties, and Covenants. The representations and warranties of Seller in this Agreement must be true in all material respects on and as of the Closing Date with the same effect as if such representations and warranties had been made on and as of the Closing Date. Seller must have performed and complied with all covenants, agreements, and conditions required by this Agreement to be performed or complied with by it before or on the Closing Date. Buyer must have been furnished with a certificate of Seller dated as of the Closing Date, certifying to the fulfillment of the foregoing conditions. Such certificate will have the effect of a representation and warranty of Seller made on and as of the Closing Date.

[*Alternative 1: Buyer's clause for delivery of estoppel certificates*]

6.1.4. Tenant Estoppel Certificates. At least _ _[*e.g., 5*]_ _ days before the Closing Date, Seller must have delivered to Buyer for its approval an updated Rent Roll dated no earlier than _ _[*e.g., 10*]_ _ days before the Closing Date (Updated Rent Roll). At least _ _[*e.g., 5*]_ _ days before the Closing Date, Seller must have delivered to Buyer an estoppel certificate from each tenant of the Property in the form attached to this

Agreement as _ _[*e.g., Exhibit E*]_ _ (Tenant Estoppel Certificates), dated no earlier than _ _[*e.g., 20*]_ _ days before the Closing Date. The Tenant Estoppel Certificates must contain no material discrepancies from the Updated Rent Roll, and must (a) confirm the terms of such tenant's lease and the current rent payable under it, (b) verify to the best knowledge of such tenant that Seller is not in default or subject to any claims or defenses of such tenant, (c) affirm that all construction obligations of landlord under such tenant's lease have been met to such tenant's satisfaction, (d) specify the amount of any deposits or prepaid rent held by Seller, (e) constitute an attornment by such tenant to Buyer and a consent to the assignment of the lease to Buyer. Despite any provisions in this Agreement to the contrary, Buyer will have until the end of the day before the Closing Date to disapprove the Updated Rent Roll and Tenant Estoppel Certificates.

[*Alternative 2: Seller's clause for delivery of estoppel certificates*]

6.1.4. Tenant Estoppel Certificates. At least _ _[*e.g., 10*]_ _ days before the Closing Date, Seller must deliver to Buyer an updated Rent Roll dated no earlier than _ _[*e.g., 30*]_ _ days before the Closing Date (Updated Rent Roll). At least _ _[*e.g., 10*]_ _ days before the Closing Date, Seller must deliver to Buyer estoppel certificates in the form attached as _ _[*e.g., Exhibit E*]_ _ or in the form required under each tenant's Lease (Tenant Estoppel Certificates), dated no earlier than _ _[*e.g., 30*]_ _ days before the Closing Date. In lieu of Tenant Estoppel Certificates from no more than _ _[*e.g., 20 percent*]_ _ of the tenants occupying no more than _ _[*e.g., 10 percent*]_ _ of the Property, Seller may substitute its own certificate verifying the information that tenant would have given under the required form of such tenant's Tenant Estoppel Certificate (Seller's Certificate). If a Tenant Estoppel Certificate or Seller's Certificate contains a material discrepancy from the Updated Rent Roll, discloses an alleged material breach by Seller as landlord under such tenant's Lease, or discloses, in Buyer's reasonable opinion, an unsatisfactory condition not discovered by Buyer during the Due Diligence Period, then Buyer may disapprove the Tenant Estoppel Certificates and the Seller Certificates and terminate this Agreement without default by either party, by giving written notice of its disapproval within _ _[*e.g., 3*]_ _ days before the Closing Date. If Buyer does not give written notice of its disapproval of the Tenant Estoppel Certificates and the Seller Certificates, then Buyer will be deemed to have approved such certificates and this Agreement will not be terminated. If at any time within _ _[*e.g., 60*]_ _ days after the Closing Date, Seller delivers a Tenant Estoppel Certificate from a tenant for which Seller previously provided a Seller's Certificate and such Tenant Estoppel Certificate contains no material discrepancies from the related Seller's Certificate, then Buyer must accept the Tenant Estoppel Certificate in lieu of the Seller's Certificate, and the Seller's Certificate will be of no further effect between Seller and Buyer.

[*Continue*]

6.1.5. Financing. The financing that Buyer must obtain as described in _ _[*e.g., section 3.6*]_ _, above, will be ready to close, and the lender that has committed to provide such financing (New Lender) must be ready to disburse the funds into Escrow as described in _ _[*e.g., section 7.4*]_ _, subject to no conditions other than conveyance of the Property by Seller to Buyer.

6.1.6. Closing Documents. Seller must have delivered to Escrow the documents and funds it is required to deliver through Escrow at Closing.

6.1.7. Physical Condition. The physical condition of the Property must be substantially the same on the Closing Date as on the Effective Date, reasonable wear and tear excepted.

6.1.8. Adverse Actions. There will exist no actions, suits, arbitrations, claims, attachments, proceedings, assignments for the benefit of creditors, insolvency, bankruptcy, reorganization, or other proceedings, pending or threatened, against Seller or regarding the Property that would materially and adversely affect Seller's ability to perform its obligations under this Agreement or Buyer's title to the Property, and there will exist no pending or threatened action, suit, or proceeding regarding the Seller before or by any court or administrative agency that seeks to restrain or prohibit, or to obtain damages or a discovery order with respect to, this Agreement or the consummation of the transactions contemplated by this Agreement.

6.1.9. Hazardous Material. No Hazardous Materials will have been discovered on the Property after the Contingency Date that were not previously disclosed to Buyer or discovered by Buyer before the Contingency Date.

6.1.10. No Material Changes. No event will have occurred nor will any condition have arisen after the Contingency Date that as of the Closing Date materially and adversely affects all or any part of the Property or its current or prospective operation, use, value, income, expenses, or occupancy.

6.1.11. Consents. All necessary agreements and consents of all parties to consummate the transaction contemplated by this Agreement will have been obtained and furnished by Seller to Buyer.

4.174-2 Seller's closing conditions

6.2. Seller's Closing Conditions. Seller's obligation to sell the Property is expressly conditioned on the fulfillment of each condition precedent at or before the Closing (Seller's Closing Conditions). Seller's Closing Conditions are solely for Seller's benefit and any of Seller's Closing Conditions may be waived in writing by Seller in whole or in part without prior notice.

6.2.1. Approval of Contingencies. It is a Seller's Closing Condition that Buyer must have acknowledged its approval or waiver of all contingencies as required under _ _[*e.g., Article 3*]_ _.

6.2.2. Purchase Price. Buyer must have delivered the Purchase Price to Escrow.

6.2.3. Delivery of Closing Documents and Funds. Buyer must have delivered to Escrow the documents and funds specified in _ _[*e.g., section 7.4*]_ _.

6.2.4. Buyer's Representations, Warranties, and Covenants. The representations and warranties of Buyer in this Agreement must be true in all material respects on and as of the Closing Date with the same effect as if such representations and warranties had been made on and as of the Closing Date. Buyer must have performed and complied with all covenants, agreements, and conditions required by this Agreement to be performed or complied with by it before or on the Closing Date. Seller must have been furnished with a certificate of Buyer dated as of the Closing Date, certifying to the fulfillment of the foregoing conditions. Such certificate will have the effect of a representation and warranty of Buyer made on and as of the Closing Date.

4.174-3 Termination for failure of a condition

6.3. Termination for Failure of a Condition. If Buyer's Closing Conditions or Seller's Closing Conditions, as the case may be, have not been previously approved or waived, this Agreement may be terminated by the party in whose favor the Closing Condition runs by written notice to the other. If this Agreement is so terminated, the parties will have no further obligation or liability under this Agreement, except as provided in _ _[*e.g., Article 9*]_ _ and this _ _[*e.g., section 6.3*]_ _. Subject to Buyer's obligations and covenants under _ _[*e.g., section 6.2*]_ _ and subject to _ _[*e.g., Article 9*]_ _, on such termination, Escrow Holder must return the Deposit to Buyer. Any cancellation fee or other costs of the Escrow Holder and Title Company will be borne equally by Seller and Buyer and each party will pay its own expenses.

Comment: On closing conditions, see §§4.121-4.131; on failure to meet conditions, see §§4.99-4.100. On the differences between the ALTA 1970 and the 1987 form policies, see California Title Insurance Practice, chap 6 (2d ed Cal CEB 1997).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.175 I. Form: Closing

§4.175 I. Form: Closing

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§4.166-4.182.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

4.175-1 Escrow

ARTICLE 7

CLOSING

7.1. Escrow. The Escrow will be opened with the Escrow Holder on the execution of this Agreement. Buyer and Seller will promptly on the Escrow Holder's request execute such additional Escrow instructions as are reasonably required to consummate the transaction contemplated by this Agreement and are not inconsistent with this Agreement.

4.175-2 Closing definitions

7.2. Closing Definitions.

7.2.1. Definition. The "Closing" means the exchange of money and documents as described in this _ _[*e.g., Article 7*]_ _, and will be deemed to have occurred when Seller's Deed to Buyer has been recorded, the Escrow Holder holds and can record and deliver the remaining documents described in this _ _[*e.g., Article 7*]_ _, the Title Company is irrevocably and unconditionally committed to issue the Title Policy, and Buyer has delivered the Purchase Price in immediately available funds to Escrow Holder.

7.2.2. Closing Date. Seller and Buyer agree that the Closing will occur on the "Closing Date." The Closing Date will be a date mutually agreeable to Buyer and Seller that is no later than _ _[*e.g., 15*]_ _ days after the Contingency Date. If the Closing has not occurred within _ _[*e.g., 15*]_ _ days after the Contingency Date, then subject to _ _[*e.g., section 6.3*]_ _ either party may elect to terminate this Agreement, the Deposit will be returned to Buyer, and neither party will have any obligations to the other except on account of any breach of this Agreement. The Closing will be at the offices of Escrow Holder or such other place as the parties may agree.

4.175-3 Seller's deposit of documents and funds

7.3. Seller's Deposit of Documents and Funds. Seller must deposit into Escrow the following documents duly executed by Seller in form and substance reasonably satisfactory to Buyer:

7.3.1. Deed. The duly executed and acknowledged Deed conveying the Property to Buyer subject only to the Permitted Exceptions;

7.3.2. Bill of Sale. A duly executed bill of sale, in the form attached to this Agreement as _ _[*e.g., Exhibit F*]_ _, conveying the Personal Property to Buyer free and clear of liens, encumbrances, and restrictions of every kind and description (Bill of Sale);

7.3.3. Assignment. A duly executed assignment, in the form attached to this Agreement as _ _[*e.g., Exhibit G*]_ _, assigning to Buyer Seller's interest (a) in the Plans (if any), (b) in all warranties of which Seller is the beneficiary with respect to the Improvements or Personal Property, (c) in all intangible assets of the Property, and (d) in such service contracts and other agreements as Buyer elects to assume (Assignment);

7.3.4. Lease Assignment. A duly executed assignment of Leases, in the form attached to this Agreement as _ _[*e.g., Exhibit H*]_ _, assigning to Buyer Seller's interest as lessor in all the Leases (Lease

Assignment);

7.3.5. Nonforeign Certification. Certificates required by §1445 of the Internal Revenue Code of 1986, and the California Revenue and Taxation Code §18815, executed by Seller and in a form satisfactory to Buyer (Nonforeign Certification), to relieve Buyer of any potential transferee's withholding liability under such statutes;

7.3.6. Lender Documents. Duly executed assignment documents as Seller's lender may require with respect to the Assumed Loan;

7.3.7. Seller's Proof of Power and Authority. Such proof of Seller's authority and authorization to enter into and perform under this Agreement, and such proof of power and authority of the individuals executing or delivering any instruments, documents, or certificates on behalf of Seller to act for and bind Seller as may reasonably be required by Buyer or the Escrow Holder; and

7.3.8. Additional Documents. Such additional documents, including written Escrow instructions consistent with this Agreement, as may be necessary or desirable to convey the Property in accordance with this Agreement.

4.175-4 Buyer's deposit of documents and funds

7.4. Buyer's Deposit of Documents and Funds. Buyer must deposit into Escrow the following funds and documents duly executed by Buyer in form and substance reasonably satisfactory to Seller:

7.4.1. Purchase Price. The Purchase Price in accordance with _ _[*e.g., Article 2*]_ _, plus or minus prorations as provided in _ _[*e.g., section 7.7*]_ _ (including funds to be provided by the New Lender as described in _ _[*e.g., section 3.6*]_ _);

7.4.2. Assumption Documents. Duly executed assumption documents as Seller's lender may require with respect to the Assumed Loan described in _ _[*e.g., section 2.3*]_ _;

7.4.3. Seller Financing Documents. Duly executed loan and security documents as Seller requires under _ _[*e.g., section 2.4*]_ _ on account of the Seller Financing;

7.4.4. New Lender Financing Documents. Duly executed loan and security documents as the New Lender may require with respect to the financing described in _ _[*e.g., section 3.6*]_ _;

7.4.5. Assignment. A duly executed assignment, in the form attached to this Agreement as _ _[*e.g., Exhibit G*]_ _, by which Buyer assumes Seller's interest in (a) the Plans (if any), (b) all warranties of which Seller is the beneficiary with respect to the Improvements or Personal Property, (c) all intangible assets of the Property, and (d) such service contracts and other agreements as Buyer elects to assume (Assignment);

7.4.6. Lease Assignment. A duly executed assignment of Leases, in the form attached to this Agreement as _ _[*e.g., Exhibit H*]_ _, by which Buyer assumes Seller's interest as lessor in all the Leases (Lease Assignment);

7.4.7. Buyer's Proof of Power and Authority. Such proof of Buyer's authority and authorization to enter into and perform under this Agreement, and such proof of power and authority of the individuals executing or delivering any instruments, documents, or certificates on behalf of Buyer to act for and bind Buyer, as may reasonably be required by Seller and the Escrow Holder; and

7.4.8. Conveyance Documents. Such documents, including written Escrow instructions consistent with this Agreement, as may be necessary or desirable for conveyance of the Property in accordance with this Agreement.

4.175-5 Closing

7.5. Closing. When the Escrow Holder receives all documents and funds identified in _ _[*e.g., sections 7.3 and 7.4*]_ _, and the Title Company is ready, willing, and able to issue the Title Policy, then, and only then, the Escrow Holder will close Escrow by:

7.5.1. Recording the Deed;

7.5.2. Recording any documents required to be recorded by Seller's lender with respect to the Assumed Loan;

7.5.3. Recording the documents Seller requires to be recorded under _ _[*e.g., section 2.4*]_ _ with respect to Seller Financing;

7.5.4. Recording any documents required to be recorded by the New Lender with respect to financing described in _ _[*e.g., section 3.6*]_ _;

7.5.5. Recording the Lease Assignment;

7.5.6. Issuing the Title Policy to Buyer;

7.5.7. Delivering to Buyer the Assignment, the Bill of Sale, the Updated Rent Roll, the original Leases, the Tenant Estoppel Certificates, the Nonforeign Certification, copies of all recorded documents related to the transfer or encumbering of the Property, the Letter of Credit, if it has not been fully drawn down under _ _[*e.g., section 2.2.4*]_ _, and a copy of Seller's Escrow instructions; and

7.5.8. Paying the Purchase Price to Seller, plus or minus prorations under _ _[*e.g., section 7.7*]_ _.

7.5.9. Thereafter, Escrow Holder will deliver signed closing statements showing all receipts and disbursements to Buyer and Seller and will file with the Internal Revenue Service (with copies to Buyer and Seller) the reporting statement required under Internal Revenue Code §6045(e).

4.175-6 Deliveries outside escrow

7.6. <u>Deliveries Outside Escrow.</u> Seller agrees to deliver the following to Buyer outside Escrow within _ _[*e.g., 3*]_ _ business days after Closing:

7.6.1. Letters in form and substance satisfactory to Buyer, signed, and stamped by Seller and addressed to each tenant at the Property, stating that the Property has been sold to Buyer and that all rents should be paid to Buyer after the Closing Date (Tenant Notices);

7.6.2. The Updated Rent Roll current through the day before the Closing Date;

7.6.3. The original Leases.

4.175-7 Prorations

7.7. <u>Prorations.</u> All receipts and disbursements of the Property will be prorated as of 11:59 p.m. on the day immediately preceding the Closing Date and the Purchase Price will be adjusted on the following basis:

7.7.1. <u>Property Rents.</u>

(a) <u>Collected Rents.</u> All rents collected by Seller under the Leases in effect on the Closing Date, including rents on account of operating cost pass-throughs, percentage rents, and other charges paid by tenants (Collected Rents) will be prorated as of the Closing by charging Seller and crediting Buyer for any Collected Rents applicable to periods after the Closing. Despite the foregoing, Collected Rents are subject to reproration for _ _[*e.g., 1*]_ _ year after the Closing Date if there is accurate and definitive evidence that Collected Rents were incorrectly applied to the preclosing or postclosing period. The party receiving such evidence must provide written notice to the other within _ _[*e.g., 5*]_ _ days after receipt of such information and the parties will reprorate the Collected Rents to adjust for any excess credit by immediate reimbursement for such excess credit. There will be no right to reprorate after the _ _[*e.g., first*]_ _ anniversary of the Closing Date.

(b) <u>Delinquent Rents.</u> All unpaid rents that are due and owed to Seller under the Leases in effect on the

Closing Date, including rents on account of operating cost pass-throughs, percentage rents, and other charges paid by tenants (Delinquent Rents) will not be prorated and will remain the property of Seller. Buyer must deliver any Delinquent Rents received by Buyer to Seller, less the actual costs of collection, on the condition that Buyer will apply all rent received from tenants under the Leases first to any obligations arising under the Leases after the Closing and Buyer will then apply the balance, if any, to the Delinquent Rents. Seller will have the right to collect Delinquent Rents, at Seller's sole cost and expense, on the condition that Seller will have no right to cause the eviction of, and Buyer will have no obligation to evict, any tenants owing Delinquent Rents.

(c) Payable Rents. All unpaid rents that have accrued under the Leases in effect on the Closing Date but that are not due and payable as of the Closing, including rents on account of operating cost pass-throughs, percentage rents, and other charges paid by tenants (Payable Rents), will be prorated as of the Closing by charging Buyer and crediting Seller for any Payable Rents applicable to periods before the Closing, as mutually agreed on by the parties not less than _ _[*e.g., 5*]_ _ days before the Closing Date. Despite the foregoing, Payable Rents are subject to reproration for _ _[*e.g., 1*]_ _ year after the Closing Date if there is accurate and definitive evidence that Payable Rents were incorrectly applied to the preclosing or postclosing period. The party receiving such evidence must provide written notice to the other within _ _[*e.g., 5*]_ _ days after receipt of such information, and the parties will reprorate the Payable Rents to adjust for any excess credit by immediate reimbursement for such excess credit. There will be no right to reprorate after the _ _[*e.g., first*]_ _ anniversary of the Closing Date.

7.7.2. Security Deposits. At Closing, Buyer will be credited and Seller will be charged with the amount of all security deposits received under the Leases in effect as of the Closing.

7.7.3. Capital Expenditures and Accounts Payable. All capital and other improvements (including labor and material) that are performed or contracted for, by or on behalf of Seller before the Closing Date, and all sums due for accounts payable that were owed or incurred by the Property before the Closing Date, must be paid by Seller.

7.7.4. Leasing Commissions. Seller must pay when due, whether before or after Closing, all leasing commissions payable with respect to Leases and extensions, renewal, and expansions of the Leases that were fully executed before the Contingency Date. Seller will be credited and Buyer will be charged the amount of leasing commissions paid by Seller on account of Leases and extensions, renewals, and expansions of the Leases that were fully executed after the Contingency Date.

7.7.5. Property Taxes. All real and personal property ad valorem taxes and special assessments, if any, whether payable in installments or not, including without limitation all supplemental taxes attributable to the period before the Closing Date for the calendar year in which the Closing occurs will be prorated to the Closing Date, based on the latest available tax rate and assessed valuation.

7.7.6. Utility Charges. Charges for utilities, including water, sewer, electric, and gas, will be prorated within _ _[*e.g., 30*]_ _ days after the Closing Date based on the then most recent bills for such services. Seller must pay for all utility services to the Property for all periods before the Closing and Buyer must pay for all utility services to the Property for the Closing Date and all periods thereafter.

4.175-8 Closing costs

7.8. Closing Costs. Closing costs will be allocated as follows:

7.8.1. Seller will pay all costs associated with removing any debt encumbering the Property;

7.8.2. Escrow costs will be shared equally by Seller and Buyer;

7.8.3. Seller will pay the cost of the Title Policy;

7.8.4. Buyer will pay the cost of recording the Deed;

7.8.5. Seller will pay costs associated with assigning the Assumed Loan, including the cost of any fees charged by Seller's lender for its consent to the Assumed Loan;

7.8.6. Buyer will pay costs associated with obtaining the financing described in _ _[*e.g., section 3.6*]_ _

from the New Lender;

7.8.7. Buyer will pay any sales tax; and

7.8.8. The documentary transfer tax and any municipal transfer tax will be paid in accordance with the custom and practice in the county in which the Property is located.

4.175-9 Broker's commission; indemnity

7.9. Broker's Commission; Indemnity. Under separate agreement, Seller must pay _ _[*name*]_ _ (Broker) for its services as broker in this transaction. Neither party has had any contact or dealings regarding the Property, or any communication in connection with the subject matter of this transaction, through any licensed real estate broker or person, other than the Broker, who can claim a commission or finder's fee as a procuring cause of the sale contemplated in this Agreement. If any other broker or finder perfects a claim for a commission or finder's fee based on any contract, dealings, or communication with a party (Indemnifying Party), then the Indemnifying Party must indemnify, defend, and hold the other party (Nonindemnifying Party) harmless from all costs and expenses (including reasonable attorney fees and costs of defense) incurred by the Nonindemnifying Party in connection with such claim.

4.175-10 Possession

7.10. Possession. Seller will deliver exclusive right of possession of the Property to Buyer on the Closing Date, subject only to the interest of tenants under the Leases.

Comment: If the buyer is not purchasing the personal property, the phrase "all personal property taxes shown on the tax bill will be paid by Seller through escrow" should be added to the proration provision. If the buyer is purchasing only some of the personal property, the parties should agree on the value of the property transferred to permit proration of the taxes. See discussion in §4.61.

For a detailed discussion of escrow and closing, see chap 15. For a form of separate buyer's escrow instructions, see §§15.48-15.61; for a form of separate seller's escrow instructions, see §§15.63-15.73. The form escrow instructions in chap 15 do not conform to the terms of this form purchase agreement.

On escrow and closing, see §§4.132-4.136.

© The Regents of the University of California

§4.176 J. Form: Risk of Loss

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§4.166-4.182.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

4.176-1 Condemnation

ARTICLE 8

RISK OF LOSS

8.1. Condemnation. If before the Closing Date any action or proceeding is commenced for the condemnation or exercise of the rights of eminent domain of the Property or any portion of it, or if Seller is notified by the duly authorized officer of a duly empowered condemning authority of the intent to commence such action or proceeding (Condemnation) and if such Condemnation would materially and adversely affect the use or operation of the Property, have the effect of decreasing the square footage of the Improvements, or reduce or eliminate access to the Property, then Buyer may either (a) terminate this Agreement or (b) proceed with the Closing without modifying the terms of this Agreement and without reducing the Purchase Price, on the condition that Seller must assign and turn over, and Buyer will be entitled to keep, all awards for the Condemnation that accrue to Seller. Seller may not negotiate, resist, or stipulate to any Condemnation without Buyer's written consent. Seller must notify Buyer of any notice of Condemnation of all or any portion of the Property within _ _[*e.g., 5*]_ _ days after the receipt of this notice, and Buyer must exercise its option(s) as provided in this _ _[*e.g., section 8.1*]_ _ within _ _[*e.g., 10*]_ _ days after receipt of such notice. If necessary, the Closing Date will be extended to give Buyer the full _ _[*e.g., 10*]_ _-day period to make such election.

4.176-2 Damage and destruction

8.2. Damage and Destruction. If before the Closing Date any damage or destruction of the Property, or any portion of it, will have occurred that results in an Uninsured Loss of _ _[*amount*]_ _ Dollars (_ _[*dollar amount*]_ _) or less, then at the Closing Seller must assign to Buyer the right to collect any Insurance Proceeds with respect to such loss and give Buyer a credit against the Purchase Price in the amount of such Uninsured Loss. If such damage or destruction results in an Uninsured Loss of more than _ _[*amount*]_ _ (_ _[*dollar amount*]_ _), then within _ _[*e.g., 5*]_ _ days after determination of the amount of the Insurance Proceeds Seller must elect either (a) to give Buyer a credit for the entire amount of such Uninsured Loss and assign to Buyer the right to collect any Insurance Proceeds with respect to such loss, or (b) to terminate this Agreement. Despite any such damage or destruction, the Purchase Price for the Property will not be reduced except by the credits referred to above. For purposes of this _ _[*e.g., section 8.2*]_ _, Uninsured Loss is the difference between (i) the sum of the actual cost necessary for the Seller to fully repair such damage and destruction, as determined by a qualified insurance adjuster selected by the insurance carrier providing insurance for the Property, and (ii) the total amount of Insurance Proceeds, which are the proceeds from any and all insurance with respect to the Property and/or to such loss, including without limitation fire and casualty and liability insurance. Uninsured Losses may arise because of self-insurance, deductible amounts under policies, proceeds of policies insufficient to cover the loss, risks not insured for, or otherwise. If any damage to or destruction of the Property occurs, the Closing Date will be extended until the amount of the Insurance Proceeds is determined and Seller has made any election permitted under this _ _[*e.g., section 8.2*]_ _.

Comment: On risk of loss, see §§4.137-4.139. For discussion of allocation of risk in accordance with CC §1662 and the Uniform Vendor and Purchaser Risk Act and for related forms, see §§13.3-13.14.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.177 K. Form: Remedies for Default

§4.177 K. Form: Remedies for Default

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§4.166-4.182.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

4.177-1 Buyer's default

ARTICLE 9

REMEDIES FOR DEFAULT

9.1. Buyer's Default. Buyer will be deemed to be in default under this Agreement (1) if Buyer fails, for any reason other than Seller's default under this Agreement or the failure of a condition precedent to Buyer's obligation to perform under this Agreement, to meet, comply with, or perform any covenant, agreement, or obligation required on its part within the time limits and in the manner required in this Agreement, or (2) if a material breach of any representation or warranty (made by Buyer) has occurred by reason of Buyer's actual fraud or intentional misrepresentation; provided, however, that no such default will be deemed to have occurred unless and until Seller has given Buyer written notice of this Agreement, describing the nature of the default, and Buyer has failed to cure such default within _ _[*e.g., 5*]_ _ days after the receipt of such notice (but in any event before the Closing Date, unless such default occurs after Closing).

4.177-2 Remedies for buyer's default

9.2. REMEDIES FOR BUYER'S DEFAULT. IF THE CLOSING FAILS TO OCCUR BECAUSE OF BUYER'S DEFAULT UNDER THE TERMS OF THIS AGREEMENT, BUYER WILL BE RESPONSIBLE FOR ALL CANCELLATION CHARGES REQUIRED TO BE PAID TO ESCROW HOLDER AND ANY ESCROW CHARGES. IN ADDITION, THIS AGREEMENT AND THE RIGHTS AND OBLIGATIONS OF THE PARTIES WILL TERMINATE AND THE DEPOSITS WILL BE IMMEDIATELY DELIVERED BY ESCROW HOLDER TO SELLER ON SELLER'S REQUEST. THE DEPOSITS WILL BE DEEMED LIQUIDATED DAMAGES FOR BUYER'S NONPERFORMANCE AS SELLER'S SOLE AND EXCLUSIVE REMEDY AGAINST BUYER (INCLUDING, WITHOUT LIMITATION, SELLER'S RIGHTS TO SEEK SPECIFIC PERFORMANCE OF THIS AGREEMENT AND TO RECEIVE DAMAGES) FOR BUYER'S FAILURE TO PURCHASE THE PROPERTY, WHICH SUMS WILL BE PRESUMED TO BE A REASONABLE ESTIMATE OF THE AMOUNT OF ACTUAL DAMAGES SUSTAINED BY SELLER BECAUSE OF BUYER'S BREACH OF ITS OBLIGATION TO PURCHASE THE PROPERTY. FROM THE NATURE OF THIS TRANSACTION, IT IS IMPRACTICABLE AND EXTREMELY DIFFICULT TO FIX THE ACTUAL DAMAGES THAT SELLER WOULD SUSTAIN IF BUYER BREACHES SUCH OBLIGATION. THE IMPRACTICABILITY AND DIFFICULTY OF FIXING ACTUAL DAMAGES IS CAUSED BY, WITHOUT LIMITATION, THE FACT THAT THE PROPERTY IS UNIQUE. GIVEN THE FOREGOING FACTS, AMONG OTHERS, BUYER AND SELLER AGREE THAT LIQUIDATED DAMAGES ARE PARTICULARLY APPROPRIATE FOR THIS TRANSACTION AND AGREE THAT SAID LIQUIDATED DAMAGES MUST BE PAID IN THE EVENT OF BUYER'S BREACH OF ITS OBLIGATION TO PURCHASE THE PROPERTY, DESPITE ANY WORDS OR CHARACTERIZATIONS PREVIOUSLY USED OR CONTAINED IN THIS AGREEMENT IMPLYING ANY CONTRARY INTENT. THE PAYMENT OF SUCH AMOUNT AS LIQUIDATED DAMAGES IS NOT INTENDED AS A FORFEITURE OR PENALTY WITHIN THE MEANING OF CALIFORNIA CIVIL CODE §3275 OR §3369 BUT IS INTENDED TO CONSTITUTE LIQUIDATED DAMAGES TO SELLER UNDER CALIFORNIA CIVIL CODE §§1671, 1676, AND 1677. NOTHING IN THIS AGREEMENT WILL, HOWEVER, BE DEEMED TO LIMIT BUYER'S LIABILITY TO SELLER FOR DAMAGES OR INJUNCTIVE RELIEF FOR BREACH OF BUYER'S INDEMNITY OBLIGATIONS UNDER _ _[*e.g., SECTION 3.5.2*]_ _, OR FOR ATTORNEY FEES AND COSTS AS PROVIDED IN _ _[*e.g., SECTION 10.10*]_ _.

WE ACKNOWLEDGE THIS LIQUIDATED DAMAGES PROVISION:

SELLER'S INITIALS: _____

BUYER'S INITIALS: _____

4.177-3 Seller's default

9.3. <u>Seller's Default.</u> Seller will be deemed to be in default under this Agreement (1) if Seller fails, for any reason other than Buyer's default under this Agreement or the failure of a condition precedent to Seller's obligation to perform under this Agreement, to meet, comply with, or perform any covenant, agreement, or obligation required on its part within the time limits and in the manner required in this Agreement, or (2) if a material breach of any representation or warranty (made by Seller) has occurred because of Seller's actual fraud or intentional misrepresentation; provided, however, that no such default will be deemed to have occurred unless and until Buyer has given Seller written notice of the default, describing its nature, and Seller has failed to cure such default within _ _[*e.g., 5*]_ _ days after receipt of such notice (but in any event before the Closing Date, unless such default occurs after Closing).

4.177-4 Remedies on seller's default

[*Alternative 1: Buyer's clause for remedies on Seller's default*]

9.4. <u>Remedies for Seller's Default.</u> If Seller defaults in its obligations under this Agreement to sell the Property to Buyer on the Closing Date through no fault of Buyer, then Buyer at its option may have the right to specific performance of this Agreement or the right to recover the Deposit and all of its general and specific damages. If, after the Closing Date, Buyer determines that Seller has breached any representation or warranty set forth in _ _[*e.g., Article 5*]_ _, then Buyer will have the right to bring an action for general and specific damages to Buyer. If this Agreement is terminated before the Closing Date for Seller's default, then, in addition to any remedy Buyer has under this Agreement, Seller will reimburse Buyer for the costs incurred by Seller in conducting its Due Diligence.

[*Alternative 2: Seller's clause for remedies on Seller's default*]

<u>9.4. WAIVER OF RIGHT TO SPECIFIC PERFORMANCE.</u> IF SELLER FAILS TO CONVEY THE PROPERTY TO BUYER IN ACCORDANCE WITH THE PROVISIONS OF THIS AGREEMENT, AND SUCH FAILURE CONSTITUTES A DEFAULT UNDER THIS AGREEMENT, THEN BUYER WILL BE ENTITLED TO THE RETURN OF THE DEPOSIT AND ALL INTEREST ACCRUED ON THAT DEPOSIT WHILE IN ESCROW, BUT BUYER WILL NOT HAVE THE RIGHT TO RECEIVE ANY EQUITABLE RELIEF, INCLUDING WITHOUT LIMITATION THE RIGHT TO RECORD A LIS PENDENS AGAINST THE PROPERTY UNDER APPLICABLE LAW OR TO PURSUE THE SPECIFIC PERFORMANCE OF THIS AGREEMENT, BUT BUYER WILL HAVE THE RIGHT TO PURSUE AN ACTION FOR DAMAGES AGAINST SELLER RELATIVE TO SUCH DEFAULT. SELLER AND BUYER ACKNOWLEDGE THAT THEY HAVE READ AND UNDERSTAND THIS _ _[*e.g., SECTION 9.4*]_ _ AND BY THEIR INITIALS IMMEDIATELY BELOW AGREE TO BE BOUND BY ITS TERMS.

Seller's Initials: _____

Buyer's Initials: _____

4.177-5 Resolution of disputes

9.5. <u>Resolution of Disputes.</u> Controversies or claims between Seller and Buyer that arise from (a) this Agreement (including any modifications to this agreement), (b) any document, agreement, or procedure related to or delivered in connection with this Agreement or the Property, (c) any violation of this Agreement, or (d) any claims for damages resulting from any business conducted between Seller and Buyer, including claims for injury to persons, property, or business interests (torts) (collectively Arbitrable Disputes) will be resolved under this _ _[*e.g., section 9.5*]_ _, which will survive termination of this Agreement. Wherever this Agreement refers to arbitration as the means of resolving disputes between the parties, the parties agree to follow the procedure described immediately below before commencing arbitration procedures. The filing of a judicial action during the term of this Agreement to enforce the other party's performance under this Agreement, *e.g.,* for an order of attachment, injunction, or other remedy, will not constitute a waiver to the filing party's right or breach of the filing party's obligation to arbitrate; provided, however, that in no circumstances following the termination of this Agreement will Buyer be entitled to record a notice of pending action (lis pendens) or take other action or seek other remedies that would have the effect of clouding Seller's title or restricting Seller's ability to convey or encumber the Property, free of any claim by Buyer to the Property.

9.5.1. Arbitration of Disputes.

(a) General. Any controversies or claims between Seller and Buyer that arise from Arbitrable Disputes will be settled by arbitration in the City of _ _[*name*]_ _, California, in accordance with the Commercial Arbitration Rules (Rules of the American Arbitration Association (AAA)) if not inconsistent with other provisions of this Agreement, and judgment on the award rendered by the arbitrators may be entered in any court having jurisdiction. The parties submit to the jurisdiction of the Superior Court of the State of California, County of _ _[*name*]_ _, for purposes of confirming any such award and entering judgment. The parties further agree that, despite anything to the contrary that may now or hereafter be contained in the Rules of the AAA, this _ _[*e.g., section 9.5.1*]_ _ will control.

(b) Appointment. Within _ _[*e.g., 10*]_ _ days after receipt of a notice of arbitration (Demand) from the other party, each party will appoint one person to hear and decide the dispute. The two persons so chosen will, within _ _[*e.g., 10*]_ _ days after their appointment, appoint a third impartial arbitrator (who must be an attorney at law licensed to practice in California), and the final majority decision of the three arbitrators will be final and conclusive on the parties to this Agreement. Each appointment of an arbitrator will be deemed complete on delivery by the appointing party of written notice of appointment of that arbitrator to the _ _[*name*]_ _ Regional Office of the AAA. If either Seller or Buyer fails to designate its arbitrator within the specified period after receipt of the Demand, then the arbitrator designated by the other party will sit as the sole arbitrator and will be deemed to be the single, mutually approved arbitrator to resolve the Arbitrable Dispute. If the party-appointed arbitrators are unable to appoint an impartial arbitrator, the impartial arbitrator will be appointed under the Rules of the AAA. If the parties cannot agree on a rate of compensation for the arbitrators, they will be compensated for their services at a rate to be determined by the AAA.

(c) Costs. Except as provided in this _ _[*e.g., section 9.5.1*]_ _, each party will bear its own costs and expenses of arbitration, including, but not limited to, filing fees, attorney fees, the fees of the arbitrator appointed by the party, and costs of transcripts, and each party agrees to pay half of the compensation to be paid to the neutral arbitrator in the arbitration. The arbitrators will not have the power or competence to allocate between the parties in their award any costs, expenses, fees, or share of arbitrators' compensation.

(d) Written Opinion. The arbitrators must, on the request of either Seller or Buyer, issue a written opinion of their findings of fact and conclusions of law. On receipt by the requesting party of this written opinion, the party will have the right to file with the arbitrators a motion to reconsider, and the arbitrators must then reconsider the issues raised by this motion and either confirm or change their majority decision, which will then be final and conclusive on the parties.

(e) Applicability of Code of Civil Procedure. It is specifically contemplated and agreed by the parties that California Code of Civil Procedure §1283.05, as it may be amended from time to time, will be incorporated into, made a part of, and made applicable to the arbitration agreement in this _ _[*e.g., section 9.5.1*]_ _.

(f) Power of Arbitrators. The arbitrators will have the authority to issue any judgment or order, including punitive damages and equitable relief; provided, however, that the arbitrators' power to provide equitable relief or specific performance will be limited to disputes in connection with the administration of this agreement and will not preclude or restrict implementation of the termination provisions of this Agreement.

(g) Statute of Limitations. For purposes of the statute of limitations, the filing of an arbitration under this _ _[*e.g., section 9.5.1*]_ _ is the equivalent of the filing of a lawsuit, and any claim or controversy that may be arbitrated under this _ _[*e.g., section 9.5.1*]_ _ is subject to any applicable statute of limitations. The arbitrators will have the authority to decide whether any such claim or controversy is barred by the statute of limitations, and, if so, to dismiss the arbitration on that basis.

(h) Disagreement on Arbitrability. If the parties disagree on whether a dispute is an Arbitrable Dispute, the issue of arbitrability will be resolved by litigation unless both parties in their sole discretion agree to make the issue of arbitrability an issue to be decided by the arbitrators under this _ _[*e.g., section 9.5.1*]_ _.

9.5.2. Statutory Notice. NOTICE: BY INITIALING IN THE SPACE BELOW, YOU ARE AGREEING TO HAVE ANY DISPUTE ARISING OUT OF THE MATTERS INCLUDED IN THE "ARBITRATION OF DISPUTES" PROVISION DECIDED BY NEUTRAL ARBITRATION AS PROVIDED BY CALIFORNIA LAW AND YOU ARE GIVING UP ANY RIGHTS YOU MIGHT POSSESS TO HAVE THE DISPUTE LITIGATED IN A COURT OR JURY TRIAL. BY INITIALING IN THE SPACE BELOW, YOU ARE GIVING UP YOUR JUDICIAL RIGHTS TO DISCOVERY AND

APPEAL, UNLESS THOSE RIGHTS ARE SPECIFICALLY INCLUDED IN THE "ARBITRATION OF DISPUTES" PROVISION. IF YOU REFUSE TO SUBMIT TO ARBITRATION AFTER AGREEING TO THIS PROVISION, YOU MAY BE COMPELLED TO ARBITRATE UNDER THE AUTHORITY OF THE CALIFORNIA CODE OF CIVIL PROCEDURE. YOUR AGREEMENT TO THIS ARBITRATION PROVISION IS VOLUNTARY.

THE UNDERSIGNED HAVE READ AND UNDERSTAND THE FOREGOING AND AGREE TO SUBMIT DISPUTES ARISING OUT OF THE MATTERS INCLUDED IN THE "ARBITRATION OF DISPUTES" PROVISION TO NEUTRAL ARBITRATION.

Seller's Initials: _____

Buyer's Initials: _____

Comment: On defaults and remedies, see §§4.140-4.150.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.178 L. Form: General Provisions

§4.178 L. Form: General Provisions

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§4.166-4.182.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

4.178-1 Notices

ARTICLE 10

GENERAL

10.1. Notices. Any notices relating to this Agreement must be given in writing and will be deemed sufficiently given and served for all purposes when delivered personally, by generally recognized overnight courier service, by facsimile (provided that sender retains a printed confirmation of delivery to the facsimile number provided below), or _ _[*e.g., 3*]_ _ days after deposit in the United States mail certified or registered, return receipt requested, with postage prepaid, addressed as follows:

SELLER: _ _[*name*]_ _
_ _[*address*]_ _
Att'n: _ _[*name*]_ _
Fax No.: _ _[*number*]_ _
with a courtesy copy to _ _[*name*]_ _
_ _[*address*]_ _
Att'n: _ _[*name*]_ _
Fax No.: _ _[*number*]_ _

BUYER: _ _[*name*]_ _
_ _[*address*]_ _
Att'n: _ _[*name*]_ _
Fax No.: _ _[*number*]_ _
with a courtesy copy to _ _[*name*]_ _
_ _[*address*]_ _
Att'n: _ _[*name*]_ _
Fax No.: _ _[*number*]_ _

ESCROW HOLDER: _ _[*name*]_ _
_ _[*address*]_ _
Att'n: _ _[*name*]_ _
Fax No.: _ _[*number*]_ _

Either party may change its address by written notice to the other given in the manner set forth above.

4.178-2 Entire agreement

10.2. Entire Agreement. This Agreement and all exhibits _ _[*addenda, schedules, agreements*]_ _ **referred to in this Agreement constitute the complete, exclusive, and final statement of the terms of the agreement with respect to the sole property between buyer and seller and may not be contradicted by evidence of any prior or contemporaneous agreement. This Agreement specifically supersedes any prior written or oral agreements between the parties. The language in all parts of this Agreement will be construed as a whole in accordance with its fair meaning and without regard to California Civil Code §1654 or similar statutes. Neither party has been induced to enter into this Agreement by, and neither party is relying on, any representation or warranty outside those expressly set forth in this Agreement.**

4.178-3 Amendments and waivers

10.3. Amendments and Waivers. No addition to or modification of this Agreement will be effective unless it is made in writing and signed by the party against whom the addition or modification is sought to be enforced. The party benefited by any condition or obligation may waive the same, but such waiver will not be enforceable by another party unless it is made in writing and signed by the waiving party.

4.178-4 Invalidity of provision

10.4. Invalidity of Provision. If any provision of this Agreement as applied to either party or to any circumstance is adjudged by a court of competent jurisdiction to be void or unenforceable for any reason, this fact will in no way affect (to the maximum extent permissible by law) any other provision of this Agreement, the application of any such provision under circumstances different from those adjudicated by the court, or the validity or enforceability of this Agreement as a whole.

4.178-5 No merger

10.5. No Merger. This Agreement, each provision of it, and all warranties and representations in this Agreement will survive the Closing and will not merge in any instrument conveying title to Buyer. All representations, warranties, agreements, and obligations of the parties will, despite any investigation made by any party to this Agreement, survive Closing, and the same will inure to the benefit of and be binding on the parties' respective successors and assigns.

4.178-6 References

10.6. References. Unless otherwise indicated, (a) all article and section references are to the articles and sections of this Agreement, and (b) except where otherwise stated, all references to days are to calendar days. Whenever under the terms of this Agreement the time for performance of a covenant or condition falls on a Saturday, Sunday, or California state holiday, such time for performance will be extended to the next business day. "Business Days" means days other than Saturday, Sunday, and California state holidays. The headings used in this Agreement are provided for convenience only and this Agreement will be interpreted without reference to any headings. The date of this Agreement is for reference purposes only and is not necessarily the date on which it was entered into.

4.178-7 Governing law

10.7. Governing Law. This Agreement will be governed by the laws of the State of California applicable to contracts made by residents of the State of California and to be performed in California.

4.178-8 Confidentiality and publicity

10.8. Confidentiality and Publicity. Before the Closing, the parties must at all times keep this transaction and any documents received from each other confidential, except to the extent necessary to (a) comply with applicable law and regulations or (b) carry out the obligations set forth in this Agreement. Any such disclosure to third parties must indicate that the information is confidential and should be so treated by the third party. Before the Closing, no press release or other public disclosure may be made by either party or any of its agents concerning this transaction without the other party's prior written consent.

4.178-9 Time

10.9. Time. Time is of the essence in the performance of the parties' respective obligations under this Agreement.

4.178-10 Attorney fees

10.10. Attorney Fees. In the event of any action or proceeding to enforce a term or condition of this Agreement, any alleged disputes, breaches, defaults, or misrepresentations in connection with any provision of this Agreement or any action or proceeding in any way arising from this Agreement, including any interpleader of the Deposit by the Escrow Holder, the prevailing party in such action, or the nondismissing party when the dismissal occurs other than by a settlement, will be entitled to recover its reasonable costs and expenses,

including without limitation reasonable attorney fees and costs of defense paid or incurred in good faith. The "prevailing party," for purposes of this Agreement, will be deemed to be that party who obtains substantially the result sought, whether by settlement, dismissal, or judgment.

4.178-11 Assignment

10.11. Assignment. This Agreement will inure to the benefit of and be binding on the parties to this Agreement and their respective successors and assigns. Buyer will have the right to assign all or any portion of its interest in this Agreement, provided that Buyer gives written notice of such assignment to Seller before the Closing Date.

4.178-12 No third party beneficiaries

10.12. No Third Party Beneficiaries. Nothing in this Agreement, express or implied, is intended to confer any rights or remedies under or by reason of this Agreement on any person other than the parties to it and their respective permitted successors and assigns, nor is anything in this Agreement intended to relieve or discharge any obligation of any third person to any party to this Agreement or give any third person any right of subrogation or action over against any party to this Agreement.

4.178-13 Remedies cumulative

10.13. Remedies Cumulative. The remedies set forth in this Agreement are cumulative and not exclusive to any other legal or equitable remedy available to a party.

4.178-14 Counterparts

10.14. Counterparts. This Agreement may be executed in one or more counterparts, each of which will be deemed an original, but all of which together will constitute one and the same instrument.

4.178-15 Tax-deferred exchange

10.15. Tax-Deferred Exchange. Seller may use the proceeds from the sale of the Property to effect one (or more) tax-deferred exchange(s) under Internal Revenue Code §1031. Buyer agrees to accommodate Seller in effecting such tax-deferred exchange. Seller will have the right, expressly reserved here, to elect such tax-deferred exchange at any time before the Closing Date. Seller and Buyer agree, however, that consummation of the purchase and sale of Property under this Agreement is not conditioned on such exchange. If Seller elects to make a tax-deferred exchange, Buyer agrees to execute such additional escrow instructions, deeds, documents, agreements, or instruments to effect this exchange, provided that Buyer must incur no additional costs, expenses, or liabilities in this transaction as a result of or in connection with this exchange. Seller agrees to hold Buyer harmless of any liability, damages, or costs, including reasonable attorney fees, that may arise from Buyer's participation in such exchange.

4.178-16 Interpretation

10.16. Interpretation. Throughout this Agreement, (a) the plural and singular numbers will each be considered to include the other; (b) the masculine, feminine, and neuter genders will each be considered to include the others; (c) "shall," "will," "must," "agrees," and "covenants" are each mandatory; (d) "may" is permissive; (e) "or" is not exclusive; and (f) "includes" and "including" are not limiting.

Comment: If facts particular to the transaction cause a party to be concerned about the timing of the closing or other deadlines in the agreement, then the parties may wish to specifically describe those concerns in section 10.9, the "time is of the essence" provision. For instance, either party may be participating in an IRC §1031 exchange or may have other tax reasons for completing the sale by a certain date (*e.g.,* recognition of loss or gain at a particular time), the buyer may need to vacate its current premises by a certain date, or a seller may need the sale proceeds to pay off a matured loan or close another transaction.

For a full discussion of tax-deferred exchanges, see Real Property Exchanges (3d ed Cal CEB 2002).

On miscellaneous provisions generally, see §§4.151-4.165.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.179 M. Form: Signature

§4.179 M. Form: Signature

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§4.166-4.182.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

4.179-1 Signature

IN WITNESS WHEREOF, the parties have executed this Agreement as of the Effective Date.

SELLER: _ _[*Name of entity*]_ _**,**
a _ _[*specify, e.g., a California corporation*]_ _

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

BUYER: _ _[*Name of entity*]_ _**,**
a _ _[*specify, e.g., a California corporation*]_ _

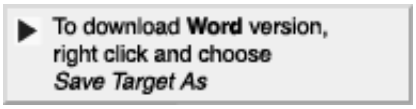
By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

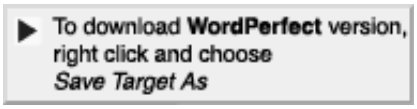
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.180 N. Form: Consent of Escrow Holder

§4.180 N. Form: Consent of Escrow Holder

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§4.166-4.182.





4.180-1 Consent of escrow holder

CONSENT OF ESCROW HOLDER

_ _[*Name*]_ _ **Title Insurance Company (Escrow Holder) accepts the foregoing Purchase and Sale Agreement and Joint Escrow Instructions as escrow instructions, agrees to act as escrow holder and agrees to be bound by their provisions applicable to it as Escrow Holder.**

Date: _ _ _ _ _ _

_ _[*Name of corporation*]_ _,
a _ _[*state of incorporation*]_ _ **corporation**

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.181 O. Form: Table of Exhibits

§4.181 O. Form: Table of Exhibits

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§4.166-4.182.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

4.181-1 Table of exhibits

TABLE OF EXHIBITS

Exhibit A	**Description of Property (see chap 11)**
Exhibit B	**Form of Note for Seller Financing (see California Real Estate Finance Practice: Strategies and Forms, chap 3 (Cal CEB 2000))**
Exhibit C	**Form of Deed of Trust for Seller Financing (see Real Estate Finance, chap 4)**
Exhibit D	**Form of Grant Deed (see App G)**
Exhibit E	**Form of Tenant Estoppel Certificate (see App K)**
Exhibit F	**Form of Bill of Sale (see App H)**
Exhibit G	**Form of Assignment (see App J)**
Exhibit H	**Form of Assignment of Leases (see App I)**
Exhibit I	**Form of Allocation of Purchase Price (see §4.182)**

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/4 The Purchase and Sale Agreement/§4.182 P. Form: Allocation of Purchase Price

§4.182 P. Form: Allocation of Purchase Price

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§4.166-4.182.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

4.182-1 Allocation of purchase price

Allocation of Purchase Price

The undersigned, _ _[*name*]_ _, a _ _[*type of entity*]_ _ (Seller), and _ _[*name*]_ _, a _ _[*type of entity*]_ _ (Buyer), entered into that certain Purchase and Sale Agreement dated as of _ _[*date*]_ _ (Agreement) for the purchase and sale of certain Property described in the Agreement. Acting under _ _[*e.g., section 2.6*]_ _ of the Agreement, the undersigned agree that the Purchase Price will be allocated as follows:

[*List the amount allocated to each of the asset classes specified in IRC §1060 that are included in the transaction, indicating "none" if no assets of that asset class were transferred. For example:*]

Cash: _ _[*dollar amount*]_ _

Land and Appurtenances: _ _[*dollar amount*]_ _;

Improvements: _ _[*dollar amount*]_ _;

Equipment: _ _[*dollar amount*]_ _;

Intangible Personal Property: _ _[*dollar amount*]_ _; **and**

Goodwill: _ _[*dollar amount*]_ _.

IN WITNESS WHEREOF, the parties have executed this Allocation of Purchase Price as of the date written below.

Dated: _ _[*date*]_ _

Seller: _ _[*NAME OF CORPORATION*]_ _,
a _ _[*state of incorporation*]_ _ **corporation**

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

Buyer: _ _[*NAME OF CORPORATION*]_ _,
a _ _[*state of incorporation*]_ _ **corporation**

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

© The Regents of the University of California

5

Specialty Commercial Purchase and Sale Agreement Provisions: Hotels

Timothy N. Brown

I. INTRODUCTION TO THE PURCHASE AND SALE OF HOTELS §5.1
- A. Nature of Hotel Operations §5.2
- B. Referral, Management, and Franchise Agreements §5.3
  - 1. Issues Involved in Franchise or Management Agreements §5.4
  - 2. Buyer's Financing §5.5
- C. Associated Resort Facilities §5.6
- D. Residential and Common Interest Arrangements §5.7

II. PURCHASE AND SALE AGREEMENT PROVISIONS
- A. Terminology §5.8
- B. Form: Definitions §5.9
- C. Assets Being Sold §5.10
- D. Form: Hotel Assets and Liabilities §5.11
- E. Buyer's Due Diligence §5.12
- F. Form: Due Diligence Documents §5.13
- G. Covenants Pending Closing §5.14
- H. Form: Seller's Pre-Closing Covenants §5.15
- I. Representations and Warranties §5.16
- J. Form: Seller's Representations and Warranties §5.17
- K. Employees §5.18
- L. Form: Employees §5.19
- M. Closing Conditions §5.20
  - 1. Required Actions by Franchisor and Manager §5.21
  - 2. Transfer of Liquor License §5.22
  - 3. Compliance With Bulk Sales Laws §5.23
  - 4. Prohibition on Material Adverse Changes §5.24
- N. Form: Closing Conditions §5.25
- O. Escrow and Closing
  - 1. Prorations §5.26
  - 2. Liquor License §5.27
  - 3. Safe Deposits and Baggage §5.28
- P. Form: Escrow and Closing §5.29

© The Regents of the University of California

§5.1 I. INTRODUCTION TO THE PURCHASE AND SALE OF HOTELS

This chapter discusses issues that arise in connection with drafting purchase and sale agreements for buying and selling hotels, motels, and resorts (referred to collectively in this chapter as hotels). Hotel sale transactions usually involve both the transfer of a large parcel of commercial property and the transfer of an operating business. The real property will have significant improvements and may include shops as well as concessions leased to third parties. Hotel sales may also include the transfer of long-term leases of apartments and suites to guests, and possibly the potential for sale of subdivided units such as condominium units within or adjacent to the hotel building. Consequently, hotel sale transactions raise all the issues present in any other major commercial real estate sale and may include residential sale aspects as well.

Hotels, however, are also operating businesses that include lodging rooms, rentals, and the operation of restaurants, bars, shops, and resort facilities. Hotel sales, therefore, also raise all the issues found in the purchase and sale of an operating business. The real estate attorney handling a hotel sale or purchase must be aware of all these issues when negotiating a purchase and sale agreement for a hotel and closing the transaction. For a general discussion of hotel sales, see *Hotels 2006: Acquiring, Managing, Developing & Converting the Hot Property* (PLI 2006).

Hotel purchase and sale agreements are almost always in the form of a conditional purchase agreement transferring the hotel's assets, similar to the form of a typical purchase agreement for any commercial property. For a commercial purchase agreement form, see §§4.166-4.182. To assist in drafting the hotel purchase and sale agreement, sample form provisions are included in this chapter to provide examples of issues that must be addressed in a hotel purchase and sale agreement.

NOTE: The form provisions in this chapter are not compatible with the form in §§4.166-4.182. Some revising would be necessary before incorporating the provisions in this chapter into the purchase and sale agreement contained in chap 4.

Transfers of hotel properties may also be concluded by merger of the ownership entity with another entity or by sale of the shares of stock or other ownership interests in the entity owning a hotel, but these types of transfers occur infrequently, owing, in large part, to issues relating to the assumption of liabilities of the transferring entity. This topic is beyond the scope of this book. For a discussion of asset sales of a business and transfers of businesses by merger or stock sale, see Sales and Mergers of California Businesses (Cal CEB 2002).

© The Regents of the University of California

§5.2 A. Nature of Hotel Operations

Hotel sale agreements must reflect the particular nature of the hotel operations conducted at the hotel being sold. Operations at minimum service "all-suite" hotels may involve few revenue generation sources other than the rental of rooms, while operations at "full-service" hotels may involve multiple revenue generation sources. Daily changes in revenue and expenses, and fluctuations in inventories of food, beverages, linens, and items for sale in shops operated by the hotel require particular attention. Often the cutoff time for calculating prorations of income and expense is 3:00 a.m. on the closing date, after the hotel bars and restaurants have closed; income and expenses before that time, and room rentals for the night ending on the closing date, are credited to the seller's account. Hotels often have numerous employees, many of whom may be employed under union contracts. A number of issues regarding employees must be resolved in the agreement, and some of these will depend on whether the employees are employed by the hotel/seller or by the hotel operator/manager. Finally, one of the most important assets of a hotel that operates food and beverage service facilities is its liquor license. Procedures for transfer of a California liquor license add another layer of complexity to a hotel transaction. See Carmichael, *Transferring Retail Liquor Licenses in California,* 15 CEB Cal Bus L Prac 65 (Summer 2000).

© The Regents of the University of California

§5.3 B. Referral, Management, and Franchise Agreements

Owners may independently manage their hotels, but this method of operation has become less common. Owners may obtain third party assistance in operating the hotel in at least four ways:

- Membership in a referral system providing access to a reservation system, a national affiliation, and perhaps the opportunity to buy supplies and services together with other owner-operators;
- Operation as part of a license or franchise system, in which the franchisor provides a variety of services and operating standards and systems;
- Leasing the hotel to an operator; or
- Hiring a management company, either as part of a hotel chain or an independent company, to manage the hotel for a fee.

In each of these arrangements, the hotel likely will be part of a chain of hotels, with a brand, often referred to as the "flag" of the hotel. See Eyster, The Negotiation and Administration of Hotel and Restaurant Management Contracts, pp. 1-20 (3d ed 1988).

Separation of ownership and management of hotels is a common method of developing and owning hotels. A national hotel chain may develop the property for a new hotel, sell the assets to an investor, enter into a franchise agreement with the investor (to put the chain's "flag" on the hotel), and require the investor to enter into a management agreement with an affiliate of the hotel chain.

© The Regents of the University of California

§5.4 1. Issues Involved in Franchise or Management Agreements

Sellers of hotels who have entered into franchise or management agreements, as well as prospective purchasers of such hotels, must consider the provisions of these agreements while planning and negotiating the sale of the hotel assets. Typical issues include:

- Should the hotel continue to operate with the same franchisor or manager?
- Is the consent of the manager or the franchisor required for the sale of the hotel? Must they approve the buyer?
- May the franchise agreement or the management agreement be terminated? Is there a termination fee?

If the manager continues to serve after the sale, many of the practical issues that could arise in closing the sale may be simplified. The manager can act as an independent third party in handling prorations and accounting issues.

© The Regents of the University of California

§5.5 2. Buyer's Financing

If the buyer will finance its purchase with a loan from a new lender, it must consider the relations between its lender and the manager and franchisor. In many respects, a lender may view the franchisor and manager in the same way as a lender on an office or retail project views the anchor tenant, as the key to the project. Important issues to be resolved include:

- Must the lender approve the existing franchisor and manager?
- Does the lender want the franchise and management agreements subordinated to its deed of trust and other security interests?
- If their agreements are subordinated to the loan, will the franchisor and manager want the lender to enter into nondisturbance agreements?

PRACTICE TIP: Based on the observations in §5.4 and above, it is clear that when drafting hotel franchise and management agreements, it is important to keep an eye on the eventual sale of the hotel. Opposing interests are at work. The franchisor and manager do not want to be replaced when the hotel changes ownership, at least not without a significant payoff. They want a say in who owns the hotel, because they have to deal with the owner over the long term. They want an experienced hotel owner who understands hotel operations. The hotel owner, however, wants the ability to sell quickly, to the party of his choosing, without having to endure a cumbersome and potentially time-consuming approval process. In addition, on foreclosure, a prospective lender wants to be able to change the manager and the franchisor, especially if the lender believes that the current ones contributed to the project's failure to generate cash flow sufficient to pay off the loan.

© The Regents of the University of California

§5.6 C. Associated Resort Facilities

Hotels are often associated with resort facilities, such as golf courses, tennis clubs, swim clubs, ski areas, and boating marinas. The relationship between the hotel and the resort facility may be structured in a number of ways. The resort facilities may be owned and operated by the hotel, or they may be separately owned and operated but associated through an arrangement that allows hotel guests to use the facilities. For example, a developer may build a hotel with a golf course, tennis courts, swimming pool, and a golf, tennis, and swim clubhouse for summer visitors and a ski area for winter visitors. After completion of the hotel and resort facilities, the developer may enter into management and franchise agreements for the hotel, sell the hotel building and assets to investors, sell the golf, tennis, and swim club to persons residing in the vicinity to be operated as a private club, and retain and operate the ski area itself. As part of the development process, the developer will enter agreements giving hotel guests the right to use the golf, tennis, and swim club and the ski facilities. These rights may be secured through recorded covenants or easements, or may simply exist contractually.

In a purchase and sale of a resort hotel, counsel for buyer and seller must identify the relationship between the hotel and the resort facilities and ensure transfer of the appropriate rights to the buyer under the purchase and sale agreement. If the hotel does not own the resort facilities, the rights for its guests to use the resort facilities must be assigned to the buyer as an asset of the hotel. If the hotel owns the resort facilities, it often makes the facilities available to members of the public on a membership basis. The membership agreements must be assigned to the buyer as an asset of the hotel. The hotel agreement forms in this chapter do not include assignment documents, but such assignments can be prepared by adapting the Assignment of Leases or the Assignment of Intangibles in Apps I-J.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/5 Specialty Commercial Purchase and Sale Agreement Provisions: Hotels/§5.7 D. Residential and Common Interest Arrangements

§5.7 D. Residential and Common Interest Arrangements

Many hotels have facilities for long-term residents, either as part of the hotel itself or affiliated with the hotel. These arrangements vary widely. Perhaps the simplest arrangement is for long-term residents to stay as hotel guests in a suite or an apartment, sometimes with leases. The Waldorf Towers in New York City is a famous example. Many hotels have been built with adjacent apartments or condominiums, whose tenants or owners have rights to use hotel facilities and services. Again, these rights may constitute encumbrances of record against the hotel or may be merely contractual in nature. Often the apartments or condominiums are in the same building as the hotel. The Four Seasons and St. Regis hotels in San Francisco are located in a portion of high-rise buildings, with the remainder of the buildings housing condominiums. In most of these examples, agreements have been entered into by which the hotel owner provides hotel services to the apartment or condominium residents, all of which must be assigned to the buyer in a sale of the hotel. It will be important to determine if there are any prohibitions, conditions, or limitations on the assignability of these service agreements.

In another type of hotel development, some or all of the hotel rooms (or suites) are sold as condominiums (with one owner of each unit), as fractional interest condominiums (with several owners of each unit, each with a right to use it for part of a year), or time-share units (sold either as real estate ownership interests having use rights for 1-week increments, either fixed by time and unit or floating among all units of a similar type, or sometimes as points-based club programs in which the units are owned or held by an owners' association or a trust for the use and benefit of the members). The hotel owner may hold only the remaining facilities needed to operate the hotel, or such facilities and a number of conventional hotel rooms or condominium units not offered separately for sale. In a conventional "condo hotel," the hotel owner owns the "hotel unit," consisting of the lobby, front desk, public rooms, meeting rooms, restaurants, and sometimes the elevators and stairways providing access to the units, and the "back-of-the-house" facilities, such as kitchens, storerooms, and laundry facilities. The hotel rooms will each be a separate condominium unit. Under the condominium documents, the hotel owner agrees to provide hotel services to the condominium owners. The services may include rental management services, with some featuring a rental pool, if a condominium owner wishes to rent the unit for some or all of the time. The manner in which the rental management program is structured and presented to the buyer, including the possible availability of a rental pool, may cause the sale of condominium units to be the sale of a security, raising issues under the federal Securities Act of 1933 (15 USC §§77a-77aa) and similar state securities laws, discussion of which is beyond the scope of this book.

NOTE: Some condo-hotel owners have brought suit against developers across the country alleging that purchasing a unit in a condo-hotel is similar to buying a stock and should, therefore, be subject to regulation by the Securities and Exchange Commission. Wall Street Journal, August 5, 2009, *The Property Report*.

The ownership structure can become more complicated if some or all of the hotel room units are sold as "time-share" units, entitling the owners to units under some form of shared use program. Time-share units themselves may be structured in a variety of ways, ranging from a fractionalized interest, under which the owner—who holds an interest in real property—is entitled to use the unit for a portion of a year (*e.g.,* "quartershares" providing 3 months of use per year, "twelfth shares" providing 4 weeks of use per year), to time-share "points," under which the units are owned by an owners' association or trust and membership in the association (or ownership of a beneficial interest in the trust) carries with it the right of the owner to use the units based on the number of points that are required to reserve a unit on any given day of the year. In California, the sale of time-share interests is regulated by the California Real Estate Commissioner under the provisions of The Vacation Ownership and Time-Share Act of 2004 (Bus & P C §§11210-11288). Accordingly, the sale of a hotel having a time-share component will present numerous additional issues for both seller's and buyer's counsel. A detailed discussion of common interest hotels is beyond the scope of this book. On timeshares, see Forming California Common Interest Developments, chap 5 (Cal CEB 2004); Muldowney and Spaulding, *Time-Share, Fractional Interest, and Vacation Club Projects: A Legal Overview*, 32 CEB Real Prop L Rep 117 (Sept. 2009); on timeshares and common interest hotels, see Hanna & Van Atta, California Common Interest

Developments, chaps 8-9 (2d ed 2002); R. Iwamoto, "Condominium Hotels," *The ACREL Papers, Spring 2006* (American College of Real Estate Lawyers and ALI-ABA 2006); C. Lisman, "Advising the Timeshare Buyer," *The ACREL Papers, Spring 2006* (American College of Real Estate Lawyers and ALI-ABA 2006); and T. Novak and J. Owen, "Condominium Hotels: Legal Structure and Allocation of Operating Expenses," *The ACREL Papers, Spring 2006* (American College of Real Estate Lawyers and ALI-ABA 2006).

© The Regents of the University of California

II. PURCHASE AND SALE AGREEMENT PROVISIONS

§5.8 A. Terminology

The hotel industry, like many, uses terms and phrases that may be unfamiliar to the real estate practitioner. For example, a "300-key hotel" means a hotel with 300 lock-off combinations of hotel rooms and suites. Many specialized hotel terms appear in hotel agreements. The description of the tangible and intangible personal property often includes much more detail regarding the various kinds of properties than is found in the sales agreements for other types of commercial property. Different types of tangible personal property either held for sale or used in the operation of the hotel are defined separately, and each type may be subject to a covenant that the seller maintain adequate stock of the items through closing. The financial reports of hotels often follow the standardized formats and account classifications contained in the American Hotel & Lodging Educational Institute's Uniform System of Accounts for the Lodging Industry (10th ed 2006).

The form in §5.9 sets forth the definitions of terms used in a typical hotel purchase and sale agreement.

© The Regents of the University of California

§5.9 B. Form: Definitions

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§5.9-5.29.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

5.9-1 Definitions

_. Definitions. The following definitions apply in this Agreement:

_.1. "Advance Booking Agreements" means contracts or agreements for Advance Bookings.

_.2. "Advance Bookings" means all agreements, bookings, or other confirmed reservations for public functions, banquets, or the use of rooms in the Hotel or other Hotel facilities or services for the period after the "Closing Date" as identified on the Advance Bookings Schedule (as that term is defined in section _ _) and all similar arrangements that Seller enters after the date of this Agreement in connection with the Hotel as permitted by section _ _ of this Agreement.

_.3. "Agreement" means this Hotel Purchase and Sale Agreement between Seller and Buyer, providing for the purchase and sale of the Property.

_.4. "Assignment and Assumption of Intangible Property" means the Assignment and Assumption of Intangible Property, to be executed by Seller and Buyer, assigning to Buyer all of Seller's right, title, and interest in and to the Intangible Property, substantially in the form of Exhibit _ _[*e.g., A*]_ _ attached to this Agreement.

_.5. "Assignment of Management Agreement" means an Assignment and Assumption of the Management Agreement in the form of or substantially the form of the attached Exhibit _ _[*e.g., B*]_ _, with such changes as may reasonably be requested by _ _[*name of manager*]_ _ or _ _[*name of licensor or franchisor*]_ _, as the case may be.

_.6. "Books, Records, and Plans" means (a) the books, records, guest and customer lists for the Hotel, and the files, reports, surveys, studies, projections, budgets, and strategic plans of Seller in connection with the ownership operation, maintenance, and management of the Property and the Hotel; (b) plans and specifications respecting the Property; and (c) structural reviews, architectural drawings, and engineering, soil, seismic, geologic, and architectural reports, studies, and certificates, and other documents pertaining to the Improvements, including without limitation any Phase I environmental reports.

_.7. "City Ledger" means all accounts receivable of guests and patrons of the Hotel who have received hotel services but not yet paid their bills (other than the Tray (Guest) Ledger) that have been outstanding as of the Close of Escrow for not more than _ _[*e.g., ninety (90)*]_ _ days.

_.8. "Consumables" means all reserve stocks of food and beverages at the Hotel.

_.9. "Cutoff Time" means 3:00 a.m. on the Closing Date.

_.10. "Equipment Leases" means all leases or other rental agreements for the use of any of the Furniture and Equipment and Expendables, all as identified on the Equipment Lease Schedule (as that term is defined in section _ _) and those leases of Furniture and Equipment and Expendables made after the date of this Agreement in connection with the Hotel as permitted by the provisions of section _ _ of this Agreement.

_.11. "Expendables" means all blankets, linens, tableware, china, glassware, silverware, uniforms, and other goods of an expendable nature owned or leased by Seller in connection with the ownership, operation, or maintenance of the Hotel and located or customarily located at the Hotel, including those items identified on

Schedule _ _ (as that term is defined in section _ _) attached to this Agreement and such replacements as are permitted or required by this Agreement, all in such quantities as may be prescribed in this Agreement.

_.12. "Fixtures" means all fixtures affixed or attached to the Real Property or Improvements, but shall not include fixtures owned by tenants or other occupants of the Real Property.

_.13. "Furniture and Equipment" means all personal property, including telephones, typewriters, mattresses, computers, software, televisions, appliances, tools, art work, furniture, furnishings, machinery, vehicles, and other personal property and equipment owned or leased by Seller in connection with the ownership, operation, or maintenance of the Hotel located or customarily located at the Hotel (but excluding Fixtures), including those items identified on the Furniture and Equipment Schedule (as that term is defined in section _ _) and such replacements as are permitted or required by this Agreement, all in such quantities as may be prescribed in this Agreement; provided, however, that Furniture and Equipment shall not include Inventory, Consumables, or Expendables.

_.14. "Goodwill" means all goodwill related to the Property or the operation of the Hotel including, without limitation, all right, title, and interest in the telephone number and listings of the Hotel, all videotapes, films, brochures, and other advertising and promotional materials of any kind or nature used in connection with the advertising and promotion of the Hotel.

_.15. "Hotel" means that certain _ _[*e.g., 300*]_ _-key hotel building and all accessory buildings and structures owned or leased by Seller and located on the Land, commonly known as the "_ _[*name of hotel*]_ _" and located at _ _[*address*]_ _.

_.16. "House Funds" means cash on hand in the Hotel's operating accounts and in reserve accounts for Furniture and Equipment, and restricted and other cash accounts (*e.g.,* payroll accounts, replacement or reserve accounts, credit card accounts, money market accounts, petty cash bank accounts, travel agent commission accounts, and accounts for excess operating funds) maintained by Seller or the hotel operator with respect to the Hotel as of the Cutoff Time.

_.17. "Improvements" means Seller's interest in any buildings, systems, facilities, structures, fences, parking areas, machinery, equipment, apparatus, and appliances attached to and used in connection with the operation or occupancy of the Land, such as heating and air-conditioning systems, refrigeration, ventilation, garbage disposal, utility conduits, or other improvements located on the Land, including without limitation the Hotel.

_.18. "Intangible Property" means the Service Contracts, the Equipment Leases, the Reservation Deposits, the Goodwill, the Books and Records and Plans, the Advance Bookings, and the Intellectual Property.

_.19. "Intellectual Property" means all copyrights, logos, designs, trademarks, trade names, service marks, and other intellectual property used in connection with the ownership and operation of the Hotel and owned by Seller, including without limitation all rights to telephone numbers for the Hotel.

_.20. "Inventory" means all stock in trade of the Hotel and operating inventories (including stationery, office supplies, soap and other guest supplies, fuel for furnaces and cleaners, cleaning compounds and preparations, and other operational and maintenance supplies) located or customarily located at the Hotel (and which shall total at least two weeks of guestroom and office supplies and two and one-half times the daily usage of linens) and till money (which shall be calculated and treated as an adjustment item under section _ _ of this Agreement); provided, however, that Inventory shall not include Expendables or Consumables.

_.21._ "Leases" means Seller's interest, as landlord, under all leases of space in the Improvements, including without limitation all occupancy agreements, concession agreements, and restaurant operating or lease agreements.

_.22. "License Agreement" means that License and Franchise Agreement dated _ _[*date*]_ _ between _ _[*name*]_ _ as licensor and franchisor and Seller as Owner.

_.23. "Licenses and Permits" means all building and other permits, certificates, and licenses, franchises, authorizations, and approvals granted by any governmental authority obtained or held by Seller that are necessary in connection with the ownership, construction, occupancy, operation, or use of the Property and the Hotel in full compliance with all applicable laws, ordinances, and statutes, a list of which is set forth on the

Licenses and Permits Schedule (as that term is defined in section _ _).

_.24. "Liquor License" means the _ _[*describe type of license, e.g., Type 47 on-sale general or eating place liquor license*]_ _ issued to Seller by the California Department of Alcoholic Beverage Control.

_.25. "Management Agreement" means that Management Agreement dated _ _[*date*]_ _ between _ _[*name*]_ _ as Manager and Seller as Owner.

_.26. "Operations Settlement" means a final accounting of the prorations under section _ _, prepared by Seller's and Buyer's accountants during the period beginning at _ _[*e.g., 8:00 p.m.*]_ _ on the day immediately before the Cutoff Time and ending at _ _[*e.g., 8:00 a.m.*]_ _ of the day immediately following the Cutoff Time, the results of which shall be incorporated into the Operations Settlement, which shall be executed by Buyer and Seller.

_.27. "Other Property" means all other assets, properties, rights, and claims of Seller that are used or held for use in connection with the Hotel, of every kind and description, wherever located, whether tangible or intangible, vested or unvested, contingent or otherwise, as the same shall exist on the Closing Date, whether or not specifically enumerated or identified in this Agreement or in any of the exhibits or schedules annexed to or delivered under this Agreement or in any other documents provided to Buyer under this Agreement.

_.28. "Other Revenues" means all revenues earned from the operation of the Hotel, other than Room Revenues, including, without limitation, sale of food and beverages, rental of meeting and banquet rooms, telephone sales, pay television sales, valet and parking services, and other similar revenues, together with any sales tax or other taxes on such revenues.

_.29. "Personal Property" means the Tangible Property and the Intangible Property.

_.30. "Reservation Deposits" means all deposits taken from guests, groups, conventions, or others, and any other amounts prepaid in connection with services to be rendered on or after the Closing Date, as identified on Schedule _ _ to this Agreement, and all deposits and similar amounts hereafter taken by Seller in connection with the Hotel as permitted by section _ _ of this Agreement.

_.31. "Room Revenues" means all revenues from the rental of guest rooms of the Hotel (but excluding any items included in the definition of Other Revenues), together with any sales or other taxes on those revenues.

_.32. "Service Contracts" means all service contracts, maintenance agreements, and supply and other contracts for the provision of services, materials, or supplies to or for the benefit of the Hotel delivered to Buyer under the provisions of section _ _, including without limitation those listed on the Service Contract Schedule (as that term is defined in section _ _) and including any guaranties of performance and warranties, and also including those other similar agreements made after the date of this Agreement in connection with the Hotel as permitted by the provisions of section _ _ of this Agreement, provided however, that Service Contracts shall not include Equipment Leases.

_.33. "Tangible Property" means the Furniture and Equipment, the Liquor License, the Inventory, the Expendables, and the Consumables.

_.34. "Transition Period" means the period of time commencing on the Effective Date and ending on the Closing Date.

_.35. "Tray (Guest) Ledger" means any accounts of guests of the Hotel who have not checked out as of the Cutoff Time.

_.36. "Union Contracts" means union collective bargaining contracts, labor agreements, and collective bargaining agreements, together with all supplements, amendments, and modifications thereto.

Comment: This form contains examples of specialized defined terms used in the sale of a hotel. Many defined terms usually found in a sales agreement for any commercial property, however, have not been included in this form. These include definitions of terms such as Buyer, Seller, Land, Real Property (meaning the Land, the Improvements, and the Fixtures), Claims, Closing, Closing Date, Escrow Holder, Escrow Instructions, Permitted Encumbrances, Title Policy,

and many others. See the form agreement beginning at §4.166 for these and other defined terms.

For a discussion of why the Cutoff Time is typically 3:00 a.m. as set in the definitions in this provision, see §5.2.

The type of liquor license described in this provision would be used if the hotel has a restaurant. A different liquor license would be required if the hotel operated only a bar, or a separate bar in addition to a bar located with the main restaurant (*e.g.,* a poolside bar). Also, if the rooms contain minibars, there will be a different liquor license for such in-room alcoholic beverage sales.

© The Regents of the University of California

§5.10 C. Assets Being Sold

As in any asset sales agreement, all the hotel assets being sold must be described in the purchase and sale agreement. The form in §5.11, a typical hotel provision for the transfer of assets and liabilities, incorporates the definitions from §5.9 (and other defined terms usually found in a real property sales agreement). Compare §§4.31-4.34 and form 4.169-2. See Sales and Mergers of California Businesses §§11.28-11.41 (Cal CEB 2002) for similar provisions in connection with a sale of a business.

The equipment used in a hotel is frequently leased, rather than financed through a loan secured by the real and personal property. Examples of equipment that may be leased include data processing equipment, telephone systems, televisions and audio-visual equipment, restaurant stoves, refrigeration and similar equipment, and vehicles. If the equipment is leased, the asset transferred is the lessee's interest in the lease, not ownership of the equipment. See California UCC Sales and Leases, chap 19 (Cal CEB 2002) regarding equipment leasing generally. Attention must be paid to any limitations, restrictions, or consents applicable to the potential assignment of the lessee's interest in such leases.

© The Regents of the University of California

§5.11 D. Form: Hotel Assets and Liabilities

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§5.9-5.29.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

5.11-1 Hotel assets and liabilities

__. Assets and Liabilities Transferred.

_.1. <u>The Property</u>. Subject to and on the terms and conditions of this Agreement, Seller will sell to Buyer and Buyer will purchase from Seller all of Seller's right, title, and interest in the Property, which will include the Land, the Fixtures, the Improvements, the Furniture and Equipment, the Inventory, the Expendables, the Consumables, the Liquor License, the Service Contracts, the License Agreement, the Management Agreement, the Leases, the Equipment Leases, the transferable Licenses and Permits, the Reservation Deposits, the Goodwill, the Books, Records and Plans, the Advance Bookings, the Intellectual Property, and the Other Property.

_.2. <u>Liabilities Not Assumed</u>. The sale of the Property will be a transfer of assets only, and no indebtedness, accounts payable, liabilities, or obligations of whatever kind or nature (including without limitation any Claims) whether actual or contingent, incurred by Seller before or after the Effective Date or the Closing Date, will be assigned by Seller or assumed by Buyer, except for (a) any liabilities to provide hotel accommodations and services under confirmed reservations for periods subsequent to the Closing Date as permitted by the terms of this Agreement, and (b) those specific liabilities expressly assumed by Buyer in this Agreement.

Comment: Accounts receivable and accounts payable are usually not transferred to the buyer, but are prorated to the closing date. The provision also disclaims the assumption of liabilities.

© The Regents of the University of California

§5.12 E. Buyer's Due Diligence

The buyer's due diligence in purchasing a hotel includes all the subjects that must be reviewed in buying any commercial real estate property. See §§4.45-4.99 and form 4.171-5. In addition to those generally required in a commercial real estate transaction, additional documents and other materials should be delivered by the seller in a hotel transaction. A typical due diligence provision tailored for hotels is shown in §5.13. A variety of schedules listing tangible personal property to attach to the agreement is provided in form 5.17-1. See Sales and Mergers of California Businesses §§1.39-1.58 (Cal CEB 2002) for a discussion of due diligence in the purchase of a business.

The following is a list of due diligence actions undertaken in hotel acquisitions that are not generally taken in other commercial real property acquisitions:

- Review management and franchise agreements to determine the rights of the manager and franchisor and the procedure for either terminating those agreements or obtaining consents to the continuation of those agreements after the hotel's sale.
- Determine whether hotel employees are employed by the owner or by the manager and whether all or most of the employees will continue to be employed by the buyer (see §5.18), and consider the applicability of the Worker Adjustment and Retraining Notification (WARN) Act (29 USC §§2101-2109).
- Review deposits and funds that will be the buyer's liabilities after closing, such as advance room and banquet bookings, reservation deposits, and escrows maintained under a management agreement for replacement of furniture, equipment, fixtures, and other capital improvements.
- Review operating inventories of linens, supplies, food, and beverages.
- Complete a UCC search, particularly to determine whether there are any equipment leases. Most equipment lessors will file a financing statement if the lease is (or might be characterized as) a security agreement under Com C §§10101-10600. See California UCC Sales and Leases §§19.5-19.18, 19.29-19.37 (Cal CEB 2002).
- Assess the equipment and systems and review service contracts to ensure the continuing maintenance and operation of the equipment (such as restaurant equipment and data processing equipment, in addition to HVAC systems and elevators).
- Consider the applicability of the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (15 USC §18a), which requires pre-merger notification to the Federal Trade Commission for certain transactions. The Act does not apply to hotel sales unless the hotel includes casino facilities or a ski area, or, in some cases, a trademark is being transferred. Nevertheless, counsel should confirm that the transaction is not covered by the Act.
- Review any construction that will continue during the due diligence period. Many hotels are in an almost constant process of refurbishment, which can involve improvements that give rise to mechanics' lien rights. On mechanics' lien provisions in purchase and sale agreements, see §4.69. For a detailed discussion, see California Mechanics' Liens and Related Construction Remedies (3d ed Cal CEB 1998).

Comment: The court of appeal in *Steiner v Thexton* (review granted Sept. 17, 2008, S164928; superseded opinion at 163 CA4th 359, 77 CR3d 632), held that a purchase agreement is unenforceable as a unilateral option lacking consideration if the buyer has the right, without forfeiture of earnest money, to terminate the purchase agreement at any time before the expiration of the contingency period. *Steiner* may have application to all real estate sales agreements, including hotel sales agreements, that provide a buyer with a "free look" during and prior to the end of any due diligence period.

© The Regents of the University of California

§5.13 F. Form: Due Diligence Documents

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§5.9-5.29.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

5.13-1 Due diligence documents

_. Document Delivery by Seller. Within _ _[*e.g., five (5)*]_ _ days after the Effective Date, Seller will provide or cause to be provided, at Seller's expense, or make available for Buyer's review (to the extent not previously provided or made available), copies of the following documents to the extent they are in Seller's possession or control (collectively, the Preliminary Documents):

_.1. Agreements. Copies of all Leases, Service Contracts, the License Agreement, the Management Agreement, all Equipment Leases, and all other written easements, covenants, restrictions, agreements, contracts, and other documents in Seller's possession or control that affect the Property or the Hotel, including without limitation any agreements of Seller relating to the insurance, service, operation, repair, supply, advertising, promotion, sale, leasing, or management of the Property or the Hotel.

_.2. Plans. Access to copies of all existing Books, Records, and Plans.

_.3. Operating Statements. Copies of the most recent annual budget and copies of operating statements for the Hotel that will cover the following periods: (a) monthly for each calendar month of the current calendar year to date, and (b) annually for the past _ _[*e.g., five (5)*]_ _ calendar years.

_.4. Licenses. Copies of the Liquor License and all Permits and Licenses (including without limitation building permits, certificates of completion, certificates of occupancy, and environmental permits and licenses).

_.5. Employees and Employee Plans. A complete list of employees (if any), their job descriptions, and salaries, together with copies of any applicable employee pension or profit-sharing plans.

_.6. Inventories. A copy of the latest itemized lists of the Inventory, Consumables, and Expendables.

_.7. Escrow Balances. A statement of the balance in all escrows for Furniture and Equipment, Fixtures, and capital expenses under the Management Agreement.

_.8. Bookings and Deposits. A complete list of all Advance Bookings and Reservation Deposits.

_.9. Other Documents. Access to current property tax bills, and all data, correspondence, documents, agreements, waivers, notices, applications, and other records with respect to the Property and the Hotel relating to transactions with taxing authorities, governmental agencies, utilities, vendors, tenants, and others with whom Buyer may be dealing after the Closing Date.

Comment: The due diligence documents listed in this form are those appropriate for the purchase of a hotel and are in addition to those a buyer would require in other commercial real property acquisitions (*e.g.,* a survey, a preliminary report on title, documents regarding the physical condition of the improvements, and written disclosures regarding pending and threatened claims). See the form beginning at §4.151 for examples of other documents to be delivered. The time period within which documents must be delivered is often subject to negotiation. Some agreements will ease the delivery requirement by providing that documents may be delivered by the seller "as soon as practicable" after the effective date of the agreement.

© The Regents of the University of California

§5.14 G. Covenants Pending Closing

Because of the nature of the hotel business, the seller's covenants regarding the hotel's operation after execution of the agreement and pending closing are often more elaborate than standard agreements, such as those discussed in §§4.101-4.106 and included in form 4.173-1. See Sales and Mergers of California Businesses §§11.55-11.70 (Cal CEB 2002) for forms regarding a seller's obligations before closing in the sale of a business. The provisions in form 5.15-1 contain detailed requirements concerning the operation and maintenance of the hotel, including the seller's obligation to continue to solicit and accept room and banquet reservations and to market the hotel's services. The buyer typically will require the seller to keep all of the contracts and agreements affecting the hotel in place, particularly the franchisee's license agreement with the franchisor, the management agreement with the manager, the equipment leases, and any space leases. The buyer will ask the seller to provide copies of all financial information in a timely manner. The agreement will often provide that the buyer may install a "shadow management" team in the hotel to observe the management and day-to-day operations.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/5 Specialty Commercial Purchase and Sale Agreement Provisions: Hotels/§5.15 H. Form: Seller's Pre-Closing Covenants

§5.15 H. Form: Seller's Pre-Closing Covenants

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§5.9-5.29.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

5.15-1 Seller's pre-closing covenants

_. Seller's Pre-Closing Covenants. During the Transition Period, and except as otherwise consented to or approved by Buyer in writing and as contemplated by this Agreement, Seller will:

_.1. Operation of Hotel. Operate the Hotel consistent with current practice and will use reasonable best efforts to (a) cooperate with Buyer to preserve present relationships with suppliers, customers, employees, and other persons having business dealings with Seller, (b) maintain present hours of operation, (c) maintain the Hotel's good reputation, (d) maintain in full force and effect all extended coverage, fire, casualty, public liability, and fidelity policies now in effect with respect to the Property and the Hotel, and (e) take all necessary actions to comply with all closing conditions set forth in Article _ _ for which Seller is responsible and to make all deliveries at Closing and do nothing that may hinder or delay the Closing.

_.2. Maintenance. Maintain the Property, including all systems used or needed for the operation of the Hotel, in substantially the same operating condition and repair as on the Effective Date of this Agreement, continue normal operation of the Property and the Hotel, and continue normal practice with respect to normal maintenance and repairs so that the Property will, except for normal wear and tear, be of at least the same quality and quantity on the Closing Date as it was on the Effective Date, and, without limiting the foregoing, maintain the quantity and quality of Personal Property at approximately the current levels.

_.3. No Transfer. Not sell, transfer, assign, or dispose of any of the Property (other than in the ordinary course of the operation of the Hotel) or enter into any tenant lease between the Effective Date and the Closing Date without Buyer's prior written approval, which approval will not be unreasonably withheld, conditioned, or delayed.

_.4. Commitments. With respect to the Property and the operation of the Hotel:

_.4.1. Not (a) modify, extend, renew, cancel, terminate, rescind, or surrender the Management Agreement, the License Agreement, any Lease, any Equipment Lease, employment contracts, Union Contract, or Employee Plans, or reduce any security deposit under any Lease or Reservation Deposit, (b) permit any rental space that is now vacant or becomes vacant to be occupied, or (c) make any sale, transfer, assignment, or other disposition of any right or privilege accruing to Seller; provided, however, that Seller must, before Closing, terminate all Service Contracts other than those identified on the Service Contract Schedule.

_.4.2. Not make or enter into any contract or arrangement, including any series of related contracts, concerning the purchase of Inventory, Expendables, Consumables, Furniture and Equipment, or Fixtures, or the maintenance and operation of the Hotel, which involves receipts, expenditures, or the provision of services with a value of more than _ _[*e.g., $10,000*]_ _ after Closing in the aggregate, without the prior consent of Buyer, which consent will not be unreasonably conditioned or withheld and which must be given or withheld within _ _[*e.g., five (5)*]_ _ days after request.

_.4.3. Not consent to any zoning changes, or sell, transfer, assign, dispose of, or consent to the utilization of any development rights, including any air rights, for the Property, or modify or amend or consent to any modification or amendment of the Hotel's certificate of occupancy, unless any such changes or transfers are in the ordinary course of business.

_.4.4. Not make or enter into any rate agreements not in the ordinary course of business without prior notification to Buyer.

_.5. Books. Maintain the books and records of the Hotel in the usual and ordinary manner, on a basis consistent with prior years, and endeavor to comply with all governmental laws, ordinances, and regulations applicable to Seller, the Property, and the conduct of the operation of the Hotel, and perform all of Seller's obligations without default.

_.6. Information. Furnish Buyer, within _ _[*e.g., three (3)*]_ _ days after Buyer notifies Seller of the Closing Date under section _ _ of this Agreement, with the following:

_.6.1. Seller's most recent operating and financial statements regarding the Hotel's operation and lists of accounts receivable when they are prepared, and keep Buyer informed on inquiry, and on a reasonable basis, about the Hotel's business operations;

_.6.2. A statement in writing of any fact that, if existing or known on the date of this Agreement, would have been required to be set forth in or disclosed under this Agreement;

_.6.3. Updates for all schedules attached to this Agreement bringing current the information provided in the schedules, provided, however, that nothing contained in this section will permit Seller to enter into any agreement, take any action, or incur any liability except as permitted by the provisions of this Agreement;

_.6.4. A list of deposits and advance payments made by Seller before the Closing Date with respect to Property that will be received after the Closing Date; and

_.6.5. All such additional information relating to the Property and the Hotel as Buyer may reasonably request.

_.7. Alterations. Not undertake or commence any renovations of or alterations to the Hotel, or any part of the Hotel or the Property, other than those already in process or within the current year's budget (a copy of which must be provided to Buyer as a Preliminary Document) and those necessary to cure governmental violations, to comply with requirements of governmental authorities and boards of insurance underwriters, or to respond to emergency situations.

_.8. Defaults and Permits. Not knowingly perform any act or omit to perform any act, or knowingly permit any act or omission to act, that will cause a breach or default of any of Seller's contracts, commitments, obligations, including without limitation, the Leases, the License Agreement, or the Management Agreement.

_.9. Reservations Before Closing. Cause Manager under the Management Agreement to continue to solicit and accept reservations for the Hotel, including reservations for any period after the Closing Date. Any of Seller's employees or agents located at the Hotel will continue their usual sales and advertising programs and campaigns to solicit such reservations. Until the Closing, Seller's employees and agents located at the Hotel have used and must continue to use their best efforts to obtain Advance Bookings and will not book into any other hotel owned or operated by Seller or its affiliates any such business that has historically been booked as part of the Hotel.

_.10. Marketing. Cause any of Seller's employees and agents located at the Hotel to continue actively and diligently marketing and promoting the Hotel, and Seller will consult and cooperate with Buyer in connection with marketing and sale promotions.

_.11. Shadow Management. During the Transition Period, permit Buyer to establish a "shadow management" operation with respect to the Hotel. Buyer's personnel, agents, and representatives will have reasonable access during normal business hours to all books, records, and other information in the possession or control of Seller, Manager, or Seller's agents concerning the Hotel, and will have the right (at Buyer's expense) to establish duplicate books and records (whether in tangible or electronic form) in order to effect a smooth transition in the ownership and management of the Hotel. Buyer agrees that its shadow management personnel, agents, and representatives will not unreasonably interfere with the normal management and operation of the Hotel, will have no authority over the management and operations of the Hotel, and will not be deemed to have assumed management responsibilities before Closing by virtue of such shadow management.

_.12. Seller Indemnification Re Pre-Closing Acts. In addition to Seller's other indemnification obligations under this Agreement, Seller agrees to indemnify, defend, and hold Buyer, its partners, limited liability company members, shareholders, directors, officers, affiliates, representatives, employees, and agents

harmless from any and all liabilities, costs, damages, claims, suits, judgments, or expenses, including without limitation reasonable attorney fees, incurred by Buyer that arise out of or are connected with (a) Seller's failure to perform under all of the contracts, leases, and agreements of Seller assumed by Buyer, or (b) any act or omission of Seller related to the ownership or operation of the Property or the Hotel before the Closing Date that may result in Seller's liability to any third party.

Comment: The seller may want an indemnification from the buyer (similar to the one in section 12 above) as to any of buyer's activities during the conduct of the shadow management program.

© The Regents of the University of California

§5.16 I. Representations and Warranties

Seller's representations and warranties are usually the subject of careful negotiations in any purchase and sale agreement. See the discussion in §§4.107-4.120 and forms 4.173-1, Alternatives 1-2, the "as is" form 4.173-5, and the release by the buyer in form 4.173-6. In the particular case of hotel agreements, the nature and extent of the seller's representations and warranties will vary depending on whether a third party manager is involved. A typical provision for use in a hotel transaction appears in §15.17. If the hotel owner also operates the hotel, more extensive representations and warranties seem appropriate. For forms addressing disclosures in the sale of a business, see Sales and Mergers of California Businesses §§11.23-11.52 (Cal CEB 2002).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/5 Specialty Commercial Purchase and Sale Agreement Provisions: Hotels/§5.17 J. Form: Seller's Representations and Warranties

§5.17 J. Form: Seller's Representations and Warranties

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§5.9-5.29.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

5.17-1 Seller's Representations and Warranties

_. Seller's Representations and Warranties. Seller makes the following representations and warranties for the benefit of Buyer:

_.1. Ordinances. To Seller's knowledge, neither the Hotel, nor its operation, violates in any way any applicable laws, ordinances, rules, regulations, judgments, orders, or covenants, conditions, and restrictions, whether federal, state, local, foreign, or private. Seller has not received any request, either formal or informal, oral or written, that Seller modify or terminate any use of the Property or the Hotel.

_.2. Utilities. To Seller's knowledge, all water, sewer, gas, electric, cable television, satellite television, Internet service, telephone, and drainage facilities, and all other utilities required by law or by the Hotel's normal operation, are adequate to service the Hotel in its present use and to permit full compliance with all requirements of law and normal usage by the Hotel's guests.

_.3. Licenses and Permits. To Seller's knowledge, Seller has all licenses, permits, easements, and rights of way, including proof of dedication, building permits, and occupancy permits that are required from any governmental authority having jurisdiction over the Hotel, or from private parties, in order to continue the present use of the Hotel and ensure adequate vehicular and pedestrian access to the Hotel. These licenses, permits, easements, and rights-of-way will be in full force and effect as of the Closing Date.

_.4. Operating Statements. All operating statements furnished to Buyer in connection with or under this Agreement (a) are true and correct, (b) have been prepared in conformity with generally accepted accounting principles consistently applied, and (c) accurately reflect the financial position of the Hotel as of their respective dates.

_.5. Insurance and Casualties. Schedule _ _ attached to this Agreement contains a true and complete description of all insurance policies currently carried by Seller affording coverage with respect to the Hotel or the Property. Seller maintains each of such policies in effect and _ _[*, except as otherwise noted in Schedule,*]_ _ has paid all premiums due in a timely manner through the date of this Agreement. _ _[*The/To Seller's knowledge, the*]_ _ Hotel has not been materially or adversely affected in any way as a result of fire, explosion, earthquake, accident, labor trouble, requisition, or taking of property by any governmental authority, flood, rainstorm, drought, riot, act of God, or any other casualty, whether or not covered by insurance.

_.6. Claims. Schedule _ _ attached to this Agreement contains a true and correct description of all pending and, to Seller's knowledge, threatened Claims against Seller. There are no other pending Claims of which Seller has received notice to Seller's knowledge, and no threatened Claims, against Seller that in any way involve or affect Seller, the Property, or the Hotel (whether for employee or guest accidents, thefts, property damage, or otherwise). Seller will advise Buyer monthly of any claims brought against Seller, the Property, or the Hotel before Closing.

_.7. Equipment Leases. Schedule _ _ attached to this Agreement contains a true and complete listing of all Equipment Leases (including leases of other Personal Property) entered into by Seller with respect to the Property or Hotel, and in all instances Seller is the lessee under the Equipment Leases (Equipment Lease Schedule). All Equipment Leases are in full force and effect and are valid and subsisting as of the date of this Agreement without modification, except as described in schedule _ _. Seller has received no notice of default from any party to an Equipment Lease and, to Seller's knowledge, there is no outstanding default on the part of Seller or the other party or parties to such Equipment Leases, except as set forth in this schedule _ _. The

rents set forth in the Equipment Leases are the actual current rents payable under the Equipment Leases and were actually paid for the month immediately preceding the date of this Agreement. True and complete copies of the Equipment Leases and all amendments, guaranties, and other related documents have been delivered to Buyer.

_.8. Service Contracts. Schedule _ _ attached to this Agreement contains a true and correct description of the Service Contracts (Service Contract Schedule). All Service Contracts, the License Agreement, and the Management Agreement are in full force and effect and neither Seller nor, to Seller's knowledge, any other party is in default in respect of any of the terms or provisions of the Service Contracts. Except as set forth in the Service Contract Schedule, all Service Contracts are terminable by Seller on not more than _ _[*e.g., 30*]_ _ days' notice from Seller, and there are no disputes or disagreements pending or, to Seller's knowledge, threatened between Seller and any other party under any Service Contract, the License Agreement, or the Management Agreement, nor to Seller's knowledge is there any basis for such a dispute or disagreement. True and complete copies of the Service Contracts, the License Agreement, and the Management Agreement, and all amendments, guaranties, and other related documents have been delivered to Buyer.

_.9. Authorizations. To Seller's knowledge, Schedule _ _ attached to this Agreement contains a true and complete description of all Licenses and Permits held by Seller (Licenses and Permits Schedule). Seller has received no notice of any violations, except as set forth in schedule _ _. Seller is not aware of any action or proceeding for the revocation of any License or Permit or any other action or proceeding before any Governmental Authority that would affect Buyer's ability to conduct the Hotel as currently conducted after the Closing. To Seller's knowledge, no License or Permit is needed other than those set forth in the License and Permit Schedule. True and complete copies of all Licenses and Permits have been delivered to Buyer.

_.10. Inventory. The Inventory to be sold to Buyer under this Agreement will at Closing be owned by Seller free and clear of any lien, and will be lawfully and validly transferable to Buyer or another designated transferee.

_.11. Advance Bookings. Schedule _ _ (Advance Bookings Schedule) attached to this Agreement contains a true and correct description of all Advance Bookings (including without limitation all group bookings) as of the date specified in that schedule for the Hotel (including, with respect to each such booking, the name of the party making the booking, the rooms booked, a summary of the services to be provided, and the total amount billed or to be billed by Seller with respect to such booking) of which Seller has records or information. Schedule _ _ attached to this Agreement contains a true and correct description of all Reservation Deposits and any other amounts prepaid in connection with future services to be rendered in connection with the Hotel (Reservation Deposit Schedule).

_.12. Contract Rooms. Except as set forth in Schedule _ _ attached to this Agreement, there are no contract room arrangements in effect at the Hotel.

_.13. Furniture and Equipment. Schedule _ _ attached to this Agreement contains a true and complete description of all Furniture and Equipment (Furniture and Equipment Schedule).

_.14. Leases. Schedule _ _ attached to this Agreement contains a true and complete description of all Leases affecting the Property or to which the Property is subject (Lease Schedule). Seller is not party to any leases, occupancies, concessions, or tenancies except for the Leases, and there are no amendments or written or oral promises or understandings, agreements, or commitments between Seller and any tenant other than as set forth in the Leases. The Leases are in full force and effect, no rent has been paid in advance except for the current period or as otherwise stated in the Leases, and to Seller's knowledge there are no defenses, setoffs, or counterclaims for the benefit of the tenants, except as disclosed in the Leases. No breach of a Lease has been committed by Seller and Seller has not received or given notice of default under a Lease that has not been cured.

Comment: This form provides extensive representations and warranties by the seller regarding the hotel and its operations. Other seller representations and warranties regarding the real property (see forms 4.173-1—4.173-6) would also be appropriate to include in an agreement for the sale of a hotel. Note that this form contains seller representations and warranties that are favorable in their form for the buyer. Seller's counsel would want to limit the scope of these kinds of representations and warranties as appropriate for the circumstances. For example, limiting the application of many of the representations to material events, not just any event.

© The Regents of the University of California

§5.18 K. Employees

As in any operating business, employees who operate the hotel and the issues regarding those employees must be covered in the sales agreement. A typical provision covering hotel employees appears in §5.19. In contrast to an office building, operating a hotel may involve a large number of employees. The sales agreement must indicate which party is their employer. If the hotel is operated by a manager, the manager is often the employer. If the manager-employer will be replaced, or if the owner is the employer, then all the employees must be terminated. Often, most employees are rehired by the new owner or manager, with the possible exception of the hotel's senior managers.

If any employees are working under a union contract, the contract must be consulted regardless of whether the union employees will be terminated. The buyer may face a variety of collective bargaining issues that are beyond the scope of this book. See Wrongful Employment Termination Practice, chap 4 (2d ed Cal CEB 1997); Higgins, The Developing Labor Law (5th ed 2006).

If any employees will not continue in their jobs after the sale, a variety of labor and employment issues must be considered. See Advising California Employers and Employees, chap 18 (Cal CEB 2005). If 50 or more employees will be terminated, the federal Worker Adjustment and Retraining Notification Act (WARN Act) (29 USC §§2101-2109) and California law (Lab C §1401) require that notices must be given to the employees at least 60 days before termination. Calculating the number of full-time and part-time employees that will be affected requires a careful review of the statutes. See Advising Employers & Employees §§18.20-18.44. If any of the employees work under a union contract, provisions of the National Labor Relations Act (29 USC §§141-187) are relevant. See Advising Employers & Employees §§18.57-18.74. In addition to potential claims of discrimination under federal and California anti-discrimination laws (see Advising Employers & Employees, chap 15), older workers may be protected by the Older Workers Benefit Protection Act of 1990 (Pub L 101-433, 104 Stat 978), which amended the Age Discrimination in Employment Act of 1967 (ADEA) (29 USC §§621-634). See Advising Employers & Employees §§18.3-18.10.

Federal and California statutes may require that continuing health care benefits be made available to employees who are terminated. The Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA) (29 USC §§1161-1169) requires employers with at least 20 employees to offer an election of continuing health care coverage to qualified beneficiaries after involuntary termination (and other events). Some individuals receiving COBRA benefits are eligible for an extended period of benefits under the California Continuation Benefits Replacement Act (Health & S C §§1366.20-1366.29). See Advising Employers & Employees §18.45.

Some buyers will insist that all employees be terminated and that the seller be responsible for all labor and employment issues, including WARN Act notices and COBRA benefits. In other circumstances the seller will insist that the buyer offer employment and continued benefits to almost all employees, to avoid WARN Act and COBRA liability and collective bargaining issues as to those employees.

© The Regents of the University of California

§5.19 L. Form: Employees

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§5.9-5.29.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

5.19-1 Employees

_. Employees.

_.1. Manager's Employees. Buyer understands that Seller has no employees, and that _ _[*name of Manager*]**_ _ manages the Hotel and employs all employees involved in the management and operation of the Hotel, and that Seller's representations and warranties in this Agreement with respect to employees do not relate to the employees of _ _**[*name of Manager*]**_ _.**

_.2. Representation and Warranty. Seller represents and warrants that there are no other employees employed by Seller except as set forth in Schedule _ _ (Employee Schedule). Seller will provide any updated versions of the Employee Schedule to Buyer at least monthly from the date of this Agreement through and including the Closing Date.

_.3. Contracts; Labor Unions. With respect to the Hotel and the operation of the Hotel, Seller represents and warrants that Seller is not a party or subject to:

_.3.1. Any employment or consulting contract or arrangement that is not by its terms terminable at will without penalty to Seller;

_.3.2. Any plan, contract, or arrangement for bonuses or incentive compensation, deferred compensation, retirement payments, or other compensation arrangement for employees, former employees, or their survivors, dependents, and beneficiaries;

_.3.3. Any plan, contract, or arrangement not otherwise disclosed providing for any employee benefit plan, whether or not insured, for any officer or employee, former officer or employee, or their survivors, dependents, and beneficiaries; or

_.3.4. Any Union Contract or other contract or arrangement with any labor union or trade association.

_.3.5. With respect to those employees identified in the Employee Schedule, if any, Seller will not enter into any of the above before the Closing without the prior consent of Buyer _ _[*which consent will not be unreasonably withheld, conditioned, or delayed*]**_ _. To Seller's knowledge, with respect to the employees identified in the Employee Schedule, if any, no movement to designate a collective bargaining representative for any of such employees exists or is threatened and Seller will notify Buyer immediately if Seller learns of any such movement.**

_.4. Labor Disputes. To Seller's knowledge, there are no pending or threatened grievances, arbitrations, employment discrimination, or wrongful termination charges, claims, proceedings, or investigation, or other labor disputes involving Seller's employees or the Hotel that affect the Hotel or its business.

_.5. Employee Plans and Benefit Arrangements; ERISA.

_.5.1. Seller does not maintain or otherwise contribute to any "employee benefit plan" as defined in §3(3) of the federal Employee Retirement Income Security Act of 1974 (ERISA) and which is subject to Title IV of ERISA, that covers any employee or former employee of Seller (Employee Plan).

_.5.2. Seller does not maintain any form of current or deferred compensation, bonus, benefit, welfare, or

similar plan or arrangement, whether or not funded, for the benefit of any single employee or former employee or any class or classes of employees or former employees of Seller. Seller does not provide directly or indirectly group medical benefits for its former employees except benefits, if any, provided under the federal Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA).

_.5.3. Neither Seller nor any of its directors or officers nor any of their respective employees or agents, nor any "party in interest" or "disqualified person" as such terms are defined in §3 of ERISA and §4975 of the U.S. Internal Revenue Code (Code), has, with respect to any Employee Plan, engaged in or been a party to any "prohibited transaction", as such term is defined in §4975 of the Code or §406 of ERISA, in connection with which Seller or any of its partners or their respective directors or employees or any Employee Plans or related funding medium could be subject to any liability under Title I of ERISA or to a tax imposed by §4975 of the Code.

_.5.4 No Employee Plan has been terminated and Seller does not expect any such Employee Plan to be terminated within the meaning of Title IV of ERISA; with respect to any Employee Plan that is a "multi-employer plan" as defined in §4001(a)(3) of ERISA, Seller has not incurred nor does it expect to incur any withdrawal liability under Title IV of ERISA, and no such plan is in reorganization status as defined in §4241 of ERISA; with respect to any Employee Plan described in §413(c) of the Code, Seller has not incurred nor does it expect to incur any liability under Title IV of ERISA. Seller is not a "substantial employer" as defined in §4001(a)(2) of ERISA with respect to any Employee Plan, except as identified in Schedule _ _ attached to this Agreement, nor has any Employee Plan subject to Part 3 of Subtitle B of Title I of ERISA or §412 of the Code, or both, incurred any "accumulated funding deficiency" (as defined in ERISA), whether or not waived; Seller has not failed to make any contributions or pay any amounts due and owing as required by the terms of any Employee Plan; nor has there been any "reportable event" within the meaning of §4043(b), §4062(e), §4063(a) or §4041(f) of ERISA with respect to any Employee Plan (other than the transactions contemplated by this Agreement).

_.6. Termination of Employment. Effective at Closing, Seller must terminate all employees listed on the Employee Schedule (if any), without liability to Buyer. Seller will provide Buyer with evidence reasonably satisfactory to Buyer of such terminations at Closing. Seller, at its sole cost and expense, must comply with all notices and other requirements and obligations, if any, required by federal and state "plant closing" laws and other applicable laws and regulations, including without limitation the federal Worker Adjustment and Retraining Notification Act (the "WARN Act"), California Lab C §§1400-1408, and any similar laws or regulations applicable to this Agreement and the transactions contemplated under this Agreement. With respect to all such terminated employees, Seller must comply with and pay all costs and expenses of accrued but unpaid or unearned salary, vacation pay, sick leave, pension benefits, health benefits, and all other employee benefits, and continuation of health and other benefits after termination of employment, including without limitation those under the federal Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA) (29 USC §§1161-1169) and California Health & S C §§1366.20-1366.29.

_.7. Employment by Buyer. Buyer may, but will not be obligated to, offer employment to any or all of the employees on the Employee Schedule at any time. During the Transition Period, Buyer will have the right to interview applicants for employment, which may include employees listed on the Employee Schedule, and which interview process may include drug testing. Seller will provide Buyer, at no charge, with meeting facilities reasonably satisfactory to Buyer so that Buyer may engage in these interviews. Before Closing, Buyer will extend offers of employment to the employees listed on the Employee Schedule (if any) whom Buyer has elected to employ on terms and conditions satisfactory to Buyer.

_.8. No Offers of Employment. Seller and its affiliates will not offer alternative employment to any employee of Seller identified in the Employee Schedule, provided that at least _ _[*e.g., five (5)*]_ _ days before Closing Buyer will specify those employees of Seller to whom Buyer does not wish to make offers of employment, and Seller then may make offers of employment to those employees. _ _[*At no time will Seller/For a period of, e.g., 2 years/6 months following the Closing, Seller will not*]_ _ make any offers of employment to those employees to whom Buyer has made offers _ _[*and who have accepted such offers from Buyer*]_ _.

_.9. Compensation. Except with Buyer's prior written consent _ _[*which consent will not be unreasonably withheld, conditioned, or delayed*]_ _, (a) no increase will be made in the compensation or rate of compensation that is or will become payable to any employees of Seller or, during any period of employment at the Hotel, to employees of Seller identified in the Employee Schedule, and (b) except to the extent that Seller is currently contractually obligated to do so, no bonus, profit-sharing, retirement, insurance, death, fringe benefits, or other

extraordinary compensation will accrue, be set aside, or be paid to any officer or employee of Seller.

_.10. Indemnification. In addition to all other indemnification obligations of Seller under this Agreement, Seller must defend, indemnify, and hold harmless Buyer and its officers, directors, employees, shareholders, partners, limited liability company members, and affiliates from any and all claims, damages, causes of action, and liabilities (including attorney fees, costs, and expenses), with counsel reasonably acceptable to Buyer, arising out of Seller's failure to comply with the provisions of this Article or the termination of Seller's employees as provided in this Article.

Comment: These form provisions assume that a third party manager employs all the hotel employees and that the manager will continue to manage the hotel and continue to employ the employees. In many cases, however, the seller may employ a few persons and the form provisions should then require the seller to assume all liabilities under the worker protection statutes discussed §5.18. See Sales and Mergers of California Businesses §§10.53-10.55, 11.39 (Cal CEB 2002) for other examples of provisions regarding employees in an agreement for the sale of a business.

© The Regents of the University of California

§5.20 M. Closing Conditions

Hotel agreements often contain additional conditions to the buyer's obligation to close the transaction. These include provisions regarding the management and franchise agreements, the liquor license, bulk sales requirements, and the continuance of the hotel business substantially as it was conducted at the time the agreement was executed.

© The Regents of the University of California

§5.21 1. Required Actions by Franchisor and Manager

Hotel management and franchise agreements are discussed in §5.3. The buyer should insist that both the manager and the franchisor approve the buyer as a qualified transferee under the respective agreements, execute an estoppel certificate confirming that there are no defaults under the respective agreements, execute a subordination and nondisturbance agreement with the buyer's lender (if the purchase is being financed by a lender), and execute a consent to the assignment of the agreements by the seller to the buyer. A form of an estoppel certificate for a hotel management agreement is in App R.

© The Regents of the University of California

§5.22 2. Transfer of Liquor License

If the hotel holds a liquor license, as most do, the liquor license must be transferred from the seller to the buyer following the detailed requirements of the California Department of Alcoholic Beverage Control (ABC) and the Alcoholic Beverage Control Act (Bus & P C §§23000-25762). A discussion of liquor license transfers is beyond the scope of this book. See Carmichael, Transferring Retail Liquor Licenses in California, 15 CEB Cal Bus L Prac 67 (Summer 2000). Complications that arise under the Alcoholic Beverage Control Act and the ABC's regulations include the following:

- An escrow must be opened in which a portion of the purchase price must be deposited pending issuance of the license to the buyer (Bus & P C §24074);
- Detailed applications must be submitted, including background information on corporate officers and directors and on owners of a 10-percent interest in the buyer (4 Cal Code Regs §57); and
- The liquor license itself cannot be pledged as security for a loan (Bus & P C §24076).

© The Regents of the University of California

§5.23 3. Compliance With Bulk Sales Laws

In states that have adopted the Uniform Commercial Code's revised bulk sales provisions (Article 6) without change, sales of services businesses—including hotels and restaurants—are not subject to the bulk sales requirements. UCC §6-103(1)(a); see UCC Official Comment No. 1 to §6-103. California's modified provision, Com C §6103(a)(1), provides that the requirements are applicable if the seller's principal business is "that of a restaurant owner." Although there appears to be no reported California appellate decision interpreting this provision in the sale of a hotel with a restaurant, bar, and banqueting business, an interpretation of this provision may exclude such a business from the bulk sale laws. Other exclusions from the bulk sales laws exist if the seller has more than one place of business and its executive offices are outside California (Com C §6103(a)(2), (b)), or if the value of the equipment, inventory, and intangible personal property being sold exceeds $5 million (Com C §6103(c)(12)). See California UCC Sales and Leases, chap 14 (Cal CEB 2002) and Com C §§6101-6111.

© The Regents of the University of California

§5.24 4. Prohibition on Material Adverse Changes

Most real estate sale agreements contain conditions to the buyer's obligation to close that serve to assure the buyer that no material adverse change has occurred to the property. These conditions are usually expressed with respect to particular issues, such as continuation of tenant leases and the absence of an eminent domain proceeding regarding the property or damage to the property. The same concepts can be used in a hotel sale agreement, and expanded to include many facets of the hotel business, such as financial results and occupancy rates. Counsel may also include a clause providing that there must be no material adverse change to the hotel's business.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/5 Specialty Commercial Purchase and Sale Agreement Provisions: Hotels/§5.25 N. Form: Closing Conditions

§5.25 N. Form: Closing Conditions

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§5.9-5.29.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

5.25-1 Closing Conditions

_. <u>License Agreement</u>.

_.1. Buyer must have been approved by _ _[*name of hotel operator*]_ _ to operate the Hotel as a _ _[*name of hotel*]_ _ under the License Agreement and on such other terms and conditions satisfactory to Buyer in its reasonable discretion (including any property improvement program required by _ _[*name of hotel operator*]_ _ in connection with the Hotel).

_.2. At least _ _[*e.g., ten (10)*]_ _ days before the Closing Date, Seller will furnish to Buyer an estoppel certificate from _ _[*name of hotel operator*]_ _ in the form of the attached Exhibit _ _ (License Agreement Estoppel Certificate), dated no earlier than _ _[*e.g., twenty (20)*]_ _ days before the Closing Date. Buyer will have through the _ _[*e.g., fifth*]_ _ day before the Closing Date to disapprove the License Agreement Estoppel Certificate.

_.3. At least _ _[*e.g., ten (10)*]_ _ days before the Closing Date, Seller will furnish to Buyer a subordination and nondisturbance agreement executed by _ _[*name of hotel operator*]_ _ in a form reasonably acceptable to Buyer and its lender (License Agreement SNDA), dated no earlier than _ _[*e.g., twenty (20)*]_ _days before the Closing Date.

_. Management Agreement.

_.1. At least _ _[*e.g., ten (10)*]_ _ days before the Closing Date, Seller will furnish to Buyer an estoppel certificate from _ _[*name of Manager*]_ _ in the form of the attached Exhibit _ _ (Management Agreement Estoppel Certificate), dated no earlier than _ _[*e.g., twenty (20)*]_ _ days before the Closing Date. Buyer will have through the _ _[*e.g., fifth*]_ _ day before the Closing Date to disapprove the Management Agreement Estoppel Certificate.

_.2. At least _ _[*e.g., ten (10)*]_ _ days before to the Closing Date, Seller will furnish to Buyer a subordination and nondisturbance agreement executed by _ _[*name of hotel operator*]_ _ in a form reasonably acceptable to Buyer and its lender (License Agreement SNDA), dated no earlier than _ _[*e.g., twenty (20)*]_ _ days before the Closing Date.

_.3. <u>Assignments</u>. Before the Closing, Seller must have deposited into Escrow the Assignment of License Agreement duly executed by _ _[*name of hotel operator*]_ _, and the Assignment of Management Agreement duly executed by _ _[*name of Manager*]_ _.

_.4. <u>Liquor License</u>. As of the close of Escrow, the Liquor License must have been transferred to Buyer.

_.5. <u>Labor Disputes</u>. There will be no strikes, labor disputes, work stoppages, grievances, arbitrations, unfair labor practices, employment discrimination, wrongful termination charges, claims or proceedings, or other labor disputes pending or threatened in writing that would affect the intended operation of the Hotel.

_.6. <u>Consents</u>. All governmental and third party consents in connection with the transactions contemplated by this Agreement must have been obtained and all applicable waiting periods must have expired, including the consent of _ _[*name of hotel operator*]_ _ and _ _[*name of Manager*]_ _ to the assignment of the License Agreement and the Management Agreement, respectively, and their execution of the Assignment of License Agreement and Assignment of Management Agreement, respectively.

_.7. Bulk Sales. Seller will deliver evidence of its compliance with all requirements, if any, of the bulk sales laws of the State of California as set forth in California Commercial Code §§6101-6111 (Bulk Sales Laws) applicable to this transaction.

_.8. No Material Adverse Changes. During the Transition Period there will not have been any event, circumstance, or breach of this Agreement that, individually or in the aggregate, will have a material adverse change or effect on the results of income, operations, or value of the Hotel and its business, taken as a whole.

_.9. Hart-Scott-Rodino Act. This Agreement is subject to the condition that compliance with the reporting requirements of the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (15 USC §18a) is either (a) not required, or (b) required, and the necessary filing is completed with no objections being received under the Act. If the parties, or either of them, determine that this transaction is subject to the Act's reporting requirements, then each party will use its best efforts to expeditiously file a completed notification report under the Act and take all other actions necessary or advisable to comply with the Act and the rules and regulations promulgated under the Act. If such requirements or such other matters as may be required by any governmental agency having jurisdiction under the Act have been complied with by Buyer, but have not been fulfilled or satisfied by Seller to permit closing by the Closing Date, Seller will be deemed to be in default under this Agreement.

© The Regents of the University of California

O. Escrow and Closing

§5.26 1. Prorations

Prorations of income and expense and similar items are more difficult and complicated in the sales of hotels than in the usual commercial property sales, reflecting the complexity of operating a hotel. Examples of proration in the context of a hotel sale are listed below. A typical provision covering escrow and closing in a hotel sale appears in §5.29.

- Revenues in hotels change on a daily basis, and closings of hotel sales usually do not occur at the end of an accounting period. Customarily, the division of revenue occurs as of the end of a hotel's business day, which occurs after all of the facilities have closed for the night. The cutoff point is sometimes at midnight but often is at 3:00 a.m., after all the bars and restaurants have closed. Hotel room guest revenue for the night before the closing date is usually assigned to the seller, but is sometimes split between the buyer and the seller.
- Expenses, including employee expenses and benefits, are usually prorated as of the revenue cutoff time; the seller is usually responsible for all expenses before that date and time, including any continuation of benefits for terminated employees.
- A physical inventory of "consumables" (food and beverages), "expendables" (linens, tableware, china, glassware, uniforms, and similar goods), and "inventory" (stock in trade, operating inventory, and guestroom supplies) is often taken as of the cutoff time, and minimum balances in each category are specified in the agreement.
- Most hotels perform a cash count at the end of each day, which should be incorporated into the prorations; cash on hand as of the cutoff time belongs to the seller.
- Under the management agreement, funds held by the manager in escrow for future capital expenses will either be credited to seller and assigned to buyer, or paid to seller and replenished by buyer.
- A variety of taxes must be prorated as of the cutoff time, including sales taxes, local hotel taxes, and employment taxes, all of which are the seller's obligation until closing. Because the buyer is continuing the business and has potential liability for those taxes, the seller customarily indemnifies the buyer for all such liabilities arising before the cutoff time.

© The Regents of the University of California

§5.27 2. Liquor License

The escrow for the transfer of the hotel's liquor license must be coordinated with the closing and the real estate escrow. Many hotel sales agreements do not include the liquor license escrow provisions, and only require transfer of the license as a condition to the closing of the real estate sale. A complete form of liquor license escrow is not presented in this book and is beyond its scope. See Carmichael, *Transferring Retail Liquor Licenses in California,* 15 CEB Cal Bus L Prac 67 (Summer 2000). Ideally, both escrows should close at the same time. If the sale of the hotel closes before the actual transfer of the liquor license, provisions will have to be made either for the temporary service of alcoholic beverages under some form of agency created for the buyer or the buyer's operator or for the temporary suspension of beverage services until such time as the liquor license transfer is completed.

© The Regents of the University of California

§5.28 3. Safe Deposits and Baggage

Many hotels have safe deposit boxes and check baggage as a service to their guests. Sellers will wish to be relieved of responsibility for the contents of safe deposit boxes and checked baggage; buyers wish to confirm that the contents of the boxes and baggage check actually exist before taking responsibility for them. Most agreements provide for an inventory of the contents of safe deposit boxes and baggage check facilities as part of closing.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/5 Specialty Commercial Purchase and Sale Agreement Provisions: Hotels/§5.29 P. Form: Escrow and Closing

§5.29 P. Form: Escrow and Closing

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§5.9-5.29.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

5.29-1 Escrow and Closing

_. Escrow and Closing.

_.1. Prorations and Adjustments. All Room Revenues and Other Revenues and all operating expenses (*e.g.,* all utilities, etc.) that vary based on the actual operations of the Hotel will be prorated as of the Cutoff Time in accordance with the provisions set forth in section _ _. Advance payments and deposits received by Seller for guest bookings, conventions, meetings, and other Hotel commitments for the period after the Closing Date will be credited to Buyer on the Closing Date. All rents receivable from tenants of the Property earned in or attributable to the period before the Closing Date will be paid to Seller to the extent that such rents have been collected on or before the Closing Date; rents earned in or attributable to the period beginning on the Closing Date and thereafter will be paid to Buyer. Rents receivable from tenants of the Property earned in or attributable to the period before the Closing Date, but received after the Closing, will be paid to Seller. Buyer must cooperate with Seller in the collection of these rents. All amounts in the net working capital account for the hotel operations as of the Closing Date will belong to Seller, and Buyer must replenish such account at Closing or, at Seller's option, credit Seller for such amount at Closing. All operating expenses that are fixed and typically are billed or accrue on a periodic basis and are capable of proration on a per diem basis (*e.g.,* insurance, property taxes, lease rent, etc.) will be prorated as of the Cutoff Time in accordance with the provisions set forth in section _ _. For purposes of calculating prorations, Buyer will be deemed to be in title to the Property (and thus entitled to the income and responsible for the expenses) after the Cutoff Time. Any apportionments and prorations that are not expressly provided for in this Agreement will be made in accordance with customary practice in _ _[*city*]_ _, _ _[*state*]_ _. Buyer and Seller will prepare a tentative Operations Settlement not later than _ _[*e.g., three (3)*]_ _ business days before the Closing Date. Under sections _ _, any adjustments to the Purchase Price related to the Personal Property or cash to be funded into Escrow or paid as of the Close of Escrow, subject to adjustment under the final Operations Settlement, must be made by an increase in the amount funded by Buyer into Escrow and a corresponding increase in the amount to be disbursed to Seller if the prorations result in a net credit to the Seller, or by a decrease in the amount to be funded by Buyer into Escrow and a corresponding decrease in the amount to be disbursed to Seller if the prorations result in a net credit to the Buyer. A copy of the schedule of adjustments as agreed on by Buyer and Seller will be delivered to Escrow Holder before the Closing Date.

_.2. Closing Statement. Escrow Holder will prepare a closing statement on or before the Closing Date, as well as a statement of all of the cash adjustments as a result of the prorations to be made as of the Close of Escrow generally referred to in section _ _.

_.3. Operations Settlement. Buyer's and Seller's accountants will prorate Room Revenues and all Other Revenues and all variable operating expenses as of the Cutoff Time, and the results of this proration together with a statement of the Tray (Guest) Ledger, the City Ledger, credit card receivables, accounts payable, tax liabilities, cash on hand at the Hotel, Inventory, Expendables, Consumables, and the House Funds will be set forth in the Operations Settlement, subject to the following:

_.3.1. Taxes. All general real estate and ad valorem personal property taxes and assessments will be prorated as of the Cutoff Time using the latest available tax rates and assessments. Sales taxes on the sale of goods, taxes on hotel room occupancy, and all employment taxes will be allocated as of the Cutoff Time. Seller will be responsible for all general real estate and ad valorem personal property taxes, all special taxes or assessments accruing with respect to the Property, all taxes on the sale of goods and occupancy of hotel rooms, and all employment taxes for all periods before the Cutoff Time, and Buyer will be responsible for all of such taxes and assessments that accrue after the Cutoff Time. Any tax refunds or rebates that apply to periods before the Cutoff Time will be the property of Seller.

_.3.2. Utilities. Before the Close of Escrow, Seller must notify all utility companies servicing the Hotel of the anticipated change in ownership of the Hotel and request that all billings after the Close of Escrow be made to Buyer at the Hotel address. Utility meters will be read, to the extent that the utility company will do so, during the daylight hours on the calendar day immediately before the Closing Date, with charges accruing before the Cutoff Time paid by Seller and charges accruing thereafter paid by Buyer. Prepaid utility charges will be prorated on the Closing Statement. Charges for utilities that are metered, or charges for the meters that have not been read by the Closing Date, will be prorated between Buyer and Seller as of the Cutoff Time, if the proration can be reasonably estimated. If the proration cannot be estimated, then after the Close of Escrow, Seller or Buyer, as appropriate, will on receipt of such billing submit a copy of the billings to the other party, and such party must pay its prorata share of these charges to the party requesting payment within _ _[*e.g., seven (7)*]_ _ calendar days from the date of any such request. Seller will be credited and Buyer debited for all deposits previously made by Seller which the utility company in question will apply to Buyer's account.

_.3.3. Service Contracts. All income and expenses with respect to the Service Contracts that Buyer elects to assume on Closing Date will be prorated as of the Cutoff Time. Seller will receive a credit for the amount of any prepaid expenses under any Service Contacts.

_.3.4. Reservations. Buyer will honor, for its account, all reservations and Advance Bookings for dates after the Close of Escrow. Buyer authorizes Seller to continue to accept reservations for guest rooms and meeting rooms for periods after the Close of Escrow, provided the terms and conditions of the reservations are in the ordinary course of Seller's business, and Buyer agrees to honor all such reservations in accordance with their terms. Any pre-closing deposits and Reservation Deposits made to Seller with respect to confirmed reservations for dates after the Close of Escrow will be credited to Buyer. Any post-closing deposits received by Seller with respect to confirmed reservations and Reservation Deposits for dates after the Close of Escrow will be forwarded to Buyer after receipt by Seller.

_.3.5. House Funds, Tray (Guest) Ledger, and Accounts Receivable. All cash on hand in the Hotel in cash registers, cashiers' "banks", and change funds as of the Cutoff Time will remain the sole property of Seller and credited to Seller and debited to Buyer. All House Funds will remain the sole property of Seller and must be applied and returned to Seller on the Close of Escrow. All amounts in the Tray (Guest) Ledger, including charges for rooms, telephone charges, and others, accruing before the Cutoff Time will be credited to Seller at face value, and all amounts in the Tray (Guest) Ledger accruing after the Cutoff Time will belong to Buyer. The entire Tray (Guest) Ledger will then become the property of Buyer. All amounts in the City Ledger accruing before the Cutoff Time will be credited to Seller at their face amount. All accounts receivable related to customer credit card charges must be treated in the same manner as the City Ledger, other than Master Charge and Visa accounts, which will be treated in the same manner as House Funds, and will remain the property of Seller.

_.3.6. Accounts Payable and Expenses. All unpaid accounts payable and expenses relating to operations of the Hotel before Close of Escrow will be paid by Seller, or by Buyer on behalf of Seller, as the case may be, and there will be no proration or decrease in the amount to be funded into Escrow under section _ _ as a result of such payments. By way of illustration, Seller will pay (a) accounts payable and expenses relating to Personal Property, Inventory, or otherwise; (b) expenses arising from items not a part of Inventory (*e.g.,* energy, utilities, insurance, advertising, trade association dues, subscriptions, etc.); and (c) services provided (*e.g.,* by independent contractors, professionals, other consultants, vendors under Service Contracts, etc.). Buyer alone will be responsible for all accounts payable related to Personal Property, Inventory, or otherwise to the extent not yet rendered as of the Close of Escrow, providing same are incurred in the ordinary course of business and such Personal Property, Inventory, or other items are delivered, and/or such services rendered, after the Close of Escrow. In addition to the foregoing, all accounts payable and expenses relating to operations of the Property after the Close of Escrow will be paid by Buyer. Prepaid expenses with respect to all such items as of the Close of Escrow will be credited to Seller.

_.3.7. Employees. All employment compensation accrued as of the Cutoff Time must be paid by Seller. Under section _ _, on the Close of Escrow any of Seller's employees at the Hotel must be terminated by Seller, and at the option of Buyer rehired by Buyer on such terms and in such capacity as may be agreed by Buyer and each such employee, it being understood that Buyer is not assuming any accrued liabilities or obligations with respect to such employees. Any termination of such employees will be undertaken by Seller before the Close of Escrow at the sole cost, expense, and liability of Seller, including continuation of employee health benefits under state or federal law, as provided in section _ _. Employees of _ _[*name of Manager*]_ _ will

remain employees of _ _[*name of Manager*]_ _.

_.3.8. Other Costs and Expenses. Seller will pay _ _[*e.g., one-half*]_ _ of the cost for a standard CLTA owner's policy (with no endorsements). Buyer will pay all other premiums for the Title Policy and any endorsements to it required by Buyer that the Title Company is willing to issue. Seller must pay all sales taxes applicable to the sale of the Personal Property. Seller must pay any documentary or other transfer taxes applicable to the sale, if any. Seller and Buyer will share equally all other costs and charges of Escrow and any attorney fees and inspection fee charged by _ _[*name of hotel operator*]_ _ or _ _[*name of Manager*]_ _.

_.4. Consumables. As of the Cutoff Time on the Closing Date, Buyer and Seller will take an inventory of all the Consumables. All food and beverages purchased by Seller in the ordinary course of business before the Cutoff Time but delivered to the Hotel after the Cutoff Time will be deemed to have been purchased by Seller for the account of Buyer, and Buyer will pay for such food and beverages as are delivered after the Cutoff Time.

_.5. Licenses/Governmental Certificates and Approvals. Buyer will be fully responsible for, and must pay all costs and fees required to be paid in connection with, the transfer of any and all Licenses and Permits currently held by Seller, and must pay all governmental transfer and license fees in connection with all Licenses and Permits, and apply for and obtain any and all new licenses, permits, certificates, and/or approvals necessary or appropriate in connection with the Hotel's operation and the consummation of the purchase and sale of the Property, subject only to paragraph _ _[*e.g., _.3.8 (Other Costs and Expenses)*]_ _. Buyer will prosecute its applications in accordance with the rules and procedures set forth under applicable law. Seller will _ _[*, at no cost or expense to Seller,*]_ _ cooperate as may be reasonably necessary to assist Buyer in obtaining the transfer or issuance of such licenses, permits, certificates, and approvals. Buyer will use reasonable efforts to cause Seller to be released from any liability relating to any Licenses and Permits to be transferred as of the Close of Escrow.

_.6. Adjustments. If any of the payments at closing are based on estimated prorations, the parties agree to make final adjustments to such prorated amounts within _ _[*e.g., thirty (30)*]_ _ days after Closing.

_.7. Safe Deposit Boxes and Baggage Check.

_.7.1. Any baggage or other property of departed guests held by Seller will remain at the Hotel in the custody of the general manager of the Hotel (General Manager) for a period not to exceed _ _[*e.g., ninety (90)*]_ _ days after the Cutoff Time. After such period, all such baggage or property will, at the option of Seller, be removed by Seller or abandoned by Seller, and Buyer may dispose of such baggage in any manner deemed appropriate by Buyer in its sole and absolute discretion.

(a) Baggage of Guests Departing Before Cutoff Time. Regarding the baggage or other property of guests who have departed the Hotel prior to the Cutoff Time, Seller agrees to indemnify, defend, and hold Buyer harmless against all claims, losses, and liabilities that Buyer may suffer, sustain, or incur in connection with such baggage or other property, except that Buyer will be responsible for holding for said period such baggage and other property of departed guests as have been placed into the General Manager's custody as of the Cutoff Time.

(b) Baggage of Guests Departing After Cutoff Time. Regarding guests who are still in the Hotel as of the Cutoff Time, all baggage and other property of such guests that has been checked with or left in the care of Seller will be inventoried jointly by Seller and Buyer. Buyer agrees to indemnify, defend, and hold Seller harmless against all claims, losses, or liabilities that Seller may suffer, sustain, or incur with respect to such inventoried baggage arising out of acts or omissions of Buyer after the Cutoff Time. Seller agrees to indemnify, defend, and hold Buyer harmless against all claims, losses, or liabilities that Buyer may suffer, sustain, or incur with respect to such inventoried baggage arising out of the acts or omissions of Seller before the Cutoff Time and all claims with respect to baggage or other property allegedly left at the Hotel before the Cutoff Time but not so tagged and inventoried.

_.7.2. Not later than _ _[*e.g., five (5)*]_ _ days before the Cutoff Time, Seller will send, or cause the General Manager to send, written notice to guests or other persons who have safe deposit boxes at the Hotel advising of the sale of the Hotel and requesting verification or removal of the contents within _ _[*e.g., five (5)*]_ _ days. The safe deposit boxes of guests or other persons who have not responded to said written notice as of the Cutoff Time will be opened only in the presence of the General Manager and representatives of both Seller and

Buyer. The contents of all boxes opened as aforesaid will be listed at the time such boxes are opened and each such list must be signed by or on behalf of the General Manager, and Buyer will not be liable or responsible for any items claimed to have been in said boxes unless such items are included in such list. Seller agree to indemnify, defend, and hold Buyer harmless from and against any claims, losses, or liabilities that Buyer may suffer, sustain, or incur with respect to any items claimed to have been in safe deposit boxes but not included on such list. Buyer agrees to indemnify, defend, and hold Seller harmless from and against any claims, losses, or liabilities that Seller may suffer, sustain, or incur with respect to items claimed to have been in safe deposit boxes and included in such list.

_.8. Indemnification.

_.8.1. Seller agrees to defend, indemnify, and hold harmless Buyer from and against any and all loss, damage, cost, claim liability, or expense (including court costs and reasonable attorney fees) suffered or incurred by Buyer as a result of Seller's failure to pay any accounts payable or any sales, use, or occupancy taxes due in connection with the rental of rooms, the sale of goods, or the performance of services before the Cutoff Time, or arising out of any event occurring on or before the Cutoff Time, excluding any loss, damage, cost, claim liability, or expense (including court costs and reasonable attorney fees) resulting from the gross negligence or willful misconduct of Buyer, or any liability or obligation respecting the Property existing as of the Cutoff Time and not assumed by Buyer under this Agreement, except to the extent Buyer has received a credit therefor against the Purchase Price under this Agreement.

_.8.2. Buyer agrees to defend, indemnify, and hold harmless Seller from and against any and all loss, damage, cost, claim, liability, or expense (including court costs and reasonable attorney fees) suffered or incurred by Seller arising out of any events relating to the period following the Cutoff Time, excluding any loss, damage, cost, claim liability, or expense (including court costs and reasonable attorney fees) resulting from the gross negligence or willful misconduct of Seller, or any liability or obligation assumed by Buyer under this Agreement or in any agreement executed and/or delivered at the Closing, or resulting from Buyer's failure to pay any item for which it received a credit against the Purchase Price under this Agreement.

Comment: Sales tax will be payable on the sale of the hotel's tangible personal property, because the seller will hold a resale certificate and there will probably be no exemption from the requirement to pay sales tax. This form provides that the seller will pay the sales taxes. Other agreements provide for an equal division of the sales taxes between the seller and the buyer. See Sales and Mergers of California Businesses §§3.42-3.44 (Cal CEB 2002).

© The Regents of the University of California

6

Residential Purchase and Sale Transactions

Howard L. Pearlman

I. INTRODUCTION
- A. Relationship to Chapter on Purchase and Sale Agreements §6.1
- B. Attorney's Role in Residential Transactions §6.2

II. RESIDENTIAL PURCHASE AND SALE AGREEMENTS
- A. Standard Form Agreements §6.3
  - 1. Contract Interpretation §6.4
  - 2. Offer, Acceptance, and Counteroffer §6.5
  - 3. Selected Provisions of the Purchase Agreement §6.6
    - a. Description of the Property
      - (1) The Real Property §6.7
      - (2) Fixtures and Personal Property §6.8
    - b. "As Is" Clauses §6.9
    - c. Liquidated Damages and Deposit Forfeiture
      - (1) Owner-Occupied One to Four Units §6.10
        - (a) Formal Requirements §6.11
        - (b) Reasonableness §6.12
        - (c) Deposit Forfeiture §6.13
      - (2) Initial Sale of New Condominiums §6.14
    - d. Alternative Dispute Resolution §6.15
      - (1) California Arbitration Provisions
        - (a)Format and Notice Requirements §6.16
        - (b) Exclusions From Arbitration §6.17
      - (2) Federal Arbitration Act
        - (a) Preemption §6.18
        - (b) Application of State Contract Law §6.18A
    - e. Mediation and Attorney Fees §6.19
    - f. Contract Contingencies §6.20
      - (1) Conditions Precedent §6.21
      - (2) Contingency Removal §6.22
    - g. Allocations, Prorations, and Cost Estimates §6.23
- B. CAR Residential Property Forms
  - 1. Form: California Residential Purchase Agreement and Joint Escrow Instructions (CAR Form RPA-CA) §6.24
  - 2. Form: Buyer's Inspection Advisory (CAR Form BIA) §6.25
  - 3. Form: Purchase Agreement Addendum (CAR Form PAA) §6.26
  - 4. Form: Statewide Buyer and Seller Advisory (CAR Form SBSA) §6.27
  - 5. Form: Notice to Buyer to Perform (CAR Form NBP) §6.28
  - 6. Form: Short Sale Addendum (CAR Form SSA) §6.28A

III. SELLER'S DISCLOSURES §6.29
- A. Common Law Duty of Disclosure §6.30
  - 1. Materiality §6.31
    - a. Physical Property Conditions §6.31A
    - b. Other Matters §6.31B
    - c. Corrected Conditions §6.32
  - 2. Scope and Extent of Disclosure §6.32A
  - 3. Public Policy Limitations on the Duty to Disclose §6.33
- B. Statutory Disclosure Requirements §6.34
  - 1. Transfer Disclosures §6.35
    - a. Real Estate Transfer Disclosure Statement §6.36
    - b. Form: Real Estate Transfer Disclosure Statement (CC §1102.6) §6.37
    - c. Local Disclosure and Transfer Requirements
      - (1) Local Option Transfer Disclosure Statement §6.38
      - (2) Form: Local Transfer Disclosure Statement (CC §1102.6a) §6.39
      - (3) Residential Building Records Report §6.40
      - (4) "Point of Sale" Ordinances §6.41
    - d. Mello-Roos Act and 1915 Bond Act §6.42
    - e. Supplemental Property Tax Bill §6.43

f. Former Federal or State Ordnance Locations §6.44
g. Window Security Bars and Safety Release Mechanisms §6.45
h. Industrial Use Zone §6.46
i. Private Transfer Fees §6.46A
2. Natural Hazard Disclosures §6.47
a. Natural Hazard Zones §6.48
b. Natural Hazard Disclosure Statement §6.49
c. Form: Natural Hazard Disclosure Statement (CAR Form NHD) §6.50
3. Health and Safety Disclosures
a. Lead-Based Paint Disclosure §6.51
b. Earthquake Hazards §6.52
c. Environmental Hazards
(1) Mandatory Disclosure §6.53
(2) Voluntary Disclosure §6.54
d. Drug Lab Cleanup Order §6.55
e. Registered Sex Offenders ("Megan's Law") §6.56
f. Smoke Detector Compliance Statement §6.57
g. Water Heater Compliance Statement §6.58
h. Structural Pest Control Inspection Report §6.59
4. Common Interest Development Disclosures §6.60
a. Davis-Stirling Act Disclosures §6.61
b. Disclosures in First Sale of Conversion Units §6.62
c. Disclosures in First Sale of Units in a New Common Interest Development §6.63
5. New Home Sales Disclosures §6.64
6. Miscellaneous Disclosures
a. Death or Illness of Occupant of Property §6.65
b. Advisability of Title Insurance §6.66
c. FHA/HUD Inspection Disclosure §6.67
d. Flood Disaster Insurance Requirements §6.68
e. Financing Disclosures §6.69
f. Home Energy Rating Program §6.70

IV. BUYER'S DUE DILIGENCE §6.71
A. Buyer's Duty of Self-Protection §6.72
B. Buyer's Duty to Investigate §6.73
C. Scope of Buyer's Due Diligence §6.74
D. Property Inspections §6.75
1. Pest Inspection §6.76
2. Home Inspection §6.77

V. TITLE AND VESTING §6.78
A. Condition of Title §6.79
1. Recorded Interests in the Property §6.80
2. Unrecorded Interests in the Property §6.81
B. Residential Title Insurance Policies §6.82
1. Coverage Statement §6.83
2. Exceptions and Exclusions §6.84
3. Endorsements §6.85
C. Vesting of Title §6.86
1. Joint Tenancy §6.87
2. Tenancy in Common §6.88
3. Community Property §6.89
4. Registered Domestic Partners §6.90
5. Community Property With Right of Survivorship §6.91
6. Tenancy in Partnership §6.92

VI. TAX CONSIDERATIONS §6.93
A. State and Federal Withholding Taxes §6.94
B. Transfer Tax §6.95
C. Property Tax §6.96
D. Capital Gains Tax §6.97

VII. FAIR HOUSING AND ANTIDISCRIMINATION LAWS §6.98
A. Federal Law
1. Civil Rights Act of 1866 §6.99
2. Fair Housing Act §6.100
B. State Law
1. Unruh Act §6.101
2. Fair Employment and Housing Act (FEHA) §6.102
C. Senior Citizen Housing §6.103
D. Other State Antidiscrimination Laws

1. Residential Facilities and Family Day Care Homes §6.104
2. Disabled Access to Condominiums §6.105
E. Local Ordinances §6.106

VIII. SALE OF DISTRESSED PROPERTY §6.106A
A. Deeds in Lieu of Foreclosure §6.106B
B. Short Sales §6.106C
1. Standard Forms Used; Disclosure Requirements Apply §6.106D
2. Lender's Evaluation and Requirements §6.106E
3. Tax Considerations §6.106F
C. Home Equity Sales Contracts §6.107
1. Requisites for Enforceability §6.108
2. Prohibited Conduct and Remedies §6.109
D. Bank-Owned (REO) Sales §6.110
E. Form: REO Advisory (CAR Form REO) §6.111

© The Regents of the University of California

I. INTRODUCTION

§6.1 A. Relationship to Chapter on Purchase and Sale Agreements

Chapter 4 discusses purchase and sale agreements in both residential and commercial contexts and should be reviewed for its general application to residential transactions. This chapter covers additional matters that are unique to the purchase and sale of residential real estate.

© The Regents of the University of California

§6.2 B. Attorney's Role in Residential Transactions

Throughout California, residential real estate transactions are typically handled by nonlawyers. Real estate licensees, representing the seller or buyer or both, complete standard form purchase contracts, generally published by state or local Realtor® associations, to document transaction terms. Contract performance is managed by real estate licensees. Escrow is opened at a title company (in Northern California) or private escrow company (in Southern California), which, in accordance with standard form escrow instructions, handles deposits and loan pay-offs, allocates and prorates costs between the buyer and seller, prepares conveyancing documents, processes loan documents, obtains lien releases, coordinates the closing, and prepares a final settlement statement. Title companies research liens, encumbrances, and other matters recorded against the property, and ultimately issue a policy of title insurance. Appraisals and financing are arranged by the buyer directly with a lender or with the assistance of an independent mortgage broker. Property inspections are conducted by licensed pest control and home inspection companies, and certain mandatory statutory disclosures are made for the seller by third party disclosure companies.

Thus, even though nearly every aspect of a residential transaction involves legal rights and obligations, and even though it is unlawful for the nonlawyers entrusted with the transaction to render legal advice, lawyers typically do not become involved in California residential transactions unless and until a dispute arises during the course of the transaction or after closing. Nevertheless, during the transaction, lawyers can provide a valuable service by clarifying the parties' legal rights and obligations and otherwise rendering advice from the perspective of a professional who has no economic interest in consummation of the transaction. After closing, lawyers can also assist clients in resolving disputes.

To most effectively represent the client, an attorney must be familiar with the customs and practices of the relevant residential real estate brokerage community and the terms of its standard form transaction documents, the significant body of relevant federal, state and local laws, principally in the area of seller disclosures, and the underlying common law duties and obligations attendant to the sale of real property. With such knowledge, attorneys can assist at every stage of a residential transaction; they can, for example:

- Explain the provisions of the purchase contract;
- Advise on contractual performance obligations and standards;
- Draft contract language to address issues unique to the transaction;
- Advise on vesting of title;
- Review and advise on title exceptions and insurance;
- Advise on tax issues (if qualified);
- Advise on disclosures, including questions of "materiality" and statutory disclosure compliance;
- Review and advise on common interest development documents and disclosures;
- Advise on the scope of the buyer's due diligence;
- Advise on applicable antidiscrimination laws;
- Review escrow instructions for compliance with transaction terms;
- Resolve disputes between the client and his or her agent or escrow company;
- Review transaction documents after closing for completeness and accuracy; and
- Advise on post-closing disputes and strategies for cost-effective resolution.

© The Regents of the University of California

II. RESIDENTIAL PURCHASE AND SALE AGREEMENTS

§6.3 A. Standard Form Agreements

For California residential transactions, pre-printed form agreements are customarily used to document transaction terms. Perhaps the most widely used form for the sale of single-family residential property (including separate interests in common interest developments) is the California Association of Realtors'® (CAR) California Residential Purchase Agreement and Joint Escrow Instructions. See §6.24. Some local Realtor® associations publish their own pre-printed purchase contracts, which are tailored to local custom and practice. A few private companies also publish pre-printed forms.

Standard form purchase agreements contain a combination of boilerplate provisions, optional provisions that apply only if a box has been checked, provisions that apply only if they are initialed by both the buyer and seller (*e.g.,* liquidated damages and arbitration clauses), and blank lines to be filled in with specific transaction terms (*e.g.,* purchase price, contingency periods, closing date). Additional or different terms may be included in the purchase agreement by attaching and incorporating either a pre-printed addendum or a custom-drafted addendum.

The CAR form of Residential Purchase Agreement and Joint Escrow Instructions incorporates a mandatory addendum, the Buyer's Inspection Advisory (see §6.25), which advises the buyer of the importance of property inspections. The Residential Purchase Agreement and Joint Escrow Instructions also includes two optional addenda:

- The Purchase Agreement Addendum (see §6.26) allows the contracting parties, by checking a box, to incorporate pre-printed terms covering common situations such as "back-up" offers, retained possession by the seller after closing, tenant information (for rental property), second loan terms, "short sales," and court confirmation.
- The Statewide Buyer and Seller Advisory (see §6.27) advises buyer and seller on a wide range of issues relevant to the seller's disclosures and the buyer's due diligence investigation.

After the parties have executed a Residential Purchase Agreement and Joint Escrow Instructions (see §6.24), if the buyer fails to timely remove a contractual contingency or take other specified action, the seller must use the CAR form Notice to Buyer to Perform (see §6.28) and provide the buyer a specified time period within which to perform or the seller may cancel the agreement. See §6.22.

© The Regents of the University of California

§6.4 1. Contract Interpretation

Preprinted form purchase agreements are subject to statutory rules of contract interpretation. See CC §§1635-1663. As with any contract, a purchase agreement must be interpreted to carry out the mutual intention of the parties as it existed at the time of contracting. CC §1636. Other rules of construction that are often applied to interpret preprinted real estate contracts include the following:

- When a contract is partly written and partly printed, the written parts control the printed parts. CC §1651.
- Words of a contract will be given their ordinary and popular meaning unless the parties indicate an intention to give them technical or special meanings. CC §1644.
- When technical terms are used, they will be given the meaning understood by persons in the profession or business to which they relate, unless the parties indicate otherwise. CC §1645.
- If all or a material part of the property is destroyed through no fault of the buyer, or is taken by eminent domain before legal title is transferred or the buyer takes possession of the property, then the seller cannot enforce the purchase contract and the buyer is entitled to recover any portion of the purchase price already paid. If, however, the destruction or taking occurs after legal title or possession has been transferred, the buyer is not relieved of the obligation to pay the purchase price and is not entitled to recover any portion of it already paid. CC §1662.

PRACTICE TIP: When the statutory risk-of-loss rules apply, a buyer should not take possession of the property before title is transferred unless the buyer has first secured appropriate insurance coverage for the period between taking possession and the title transfer.

For further discussion regarding rules of contract interpretation, see California Law of Contracts, §§5.1-5.32 (Cal CEB 2007).

© The Regents of the University of California

§6.5 2. Offer, Acceptance, and Counteroffer

General principles of contract law govern the offer and acceptance process typically followed in residential transactions. The standard form purchase agreement is completed to reflect the terms on which the buyer proposes to purchase the property and is delivered to the seller as the purchase offer. The terms of the offer must be sufficiently definite that the performance promised is reasonably certain. *Ladas v California State Automobile Ass'n* (1993) 19 CA4th 761, 770, 23 CR2d 810. A contract for the sale of real property is sufficiently definite to be specifically enforced as long as the court can ascertain the seller, the buyer, the purchase price, the property to be transferred, and the time and manner of payment. *Patel v Liebermensch* (2008) 45 C4th 344, 349, 86 CR3d 366. If time and manner of payment are not specified in the contract, reasonable terms may be implied. 45 C4th at 350 (escrow period is not a necessary term of a real estate sales contract).

The offer typically specifies the manner of acceptance and the date and time by which acceptance must be received by the seller or agent. If these matters are specified, the offer can be effectively accepted only by the method and within the time specified. See *Palo Alto Town & Country Village, Inc. v BBTC Co.* (1974) 11 C3d 494, 498, 113 CR 705. The offer may be revoked by the offeror at any time before the offeree's acceptance has been communicated. CC §1586. To create a binding contract, acceptance must be absolute and unqualified. CC §1585. A qualified acceptance ends the original offer and constitutes a new proposal or counteroffer. *Panagotacos v Bank of America* (1998) 60 CA4th 851, 855, 70 CR2d 595; *Roth v Malson* (1998) 67 CA4th 552, 557, 79 CR2d 226 (interpreting CAR's counteroffer form).

The Residential Purchase Agreement and Joint Escrow Instructions (see §6.24) provides the seller with the options of rejecting the offer, accepting all terms of the offer, or accepting the offer "subject to" an attached counteroffer. The last option, as a conditional acceptance, becomes a new proposal that ends the original offer and does not create a binding contract unless and until properly accepted. The counteroffer should provide that the terms of the original offer are accepted subject to the other party's acceptance of the additional or different terms stated in the counteroffer. The same process of rejection, acceptance, or counteroffer continues until one of the parties unequivocally accepts the other party's terms.

PRACTICE TIP: Multiple counteroffers are common in residential transactions before the parties agree on essential terms such as purchase price, length of contingency periods, and the date for close of escrow. Counteroffers are often drafted quickly and exchanged by fax or e-mail. Because such terms are customized and handwritten, they supersede the pre-printed form if there is any conflict. Accordingly, the parties should make sure that the newly proposed written terms do not conflict with pre-printed terms unless they intend the written terms to supersede. In that situation, the best practice is to reference on the counteroffer form the paragraph of the pre-printed form that the new written term is intended to replace, *e.g.,* "The purchase price in paragraph 1.C shall be $500,000." Similarly, paragraphs the parties agree to delete from the purchase agreement should be specifically referenced in the counteroffer.

© The Regents of the University of California

§6.6 3. Selected Provisions of the Purchase Agreement

Selected provisions of a residential purchase agreement that are commonly disputed are discussed in §§6.7-6.23. Legal analysis and advice can help resolve these disputes. The discussion refers to the California Residential Purchase Agreement and Joint Escrow Instructions set forth in §6.24. Other forms typically include similar provisions, but they may differ materially and should be carefully reviewed.

© The Regents of the University of California

a. Description of the Property

§6.7 (1) The Real Property

By definition, real property consists of land, fixtures, rights appurtenant to land (*i.e.,* used with the land for its benefit) such as easements, and things that are immovable by law. CC §658. Every other kind of property is personal property. CC §663. In every residential transaction, the purchase agreement should specifically identify the real property and any personal property interests being transferred.

The real property is typically identified by street address, city, county, and assessor's parcel number. A preliminary title report will include a legal description of the real property and will identify any appurtenances as well as liens and encumbrances. See §6.80.

In a residential transaction a survey confirming the boundaries of the property is rarely performed, even though disputes regarding boundaries, encroachments, and easements frequently arise. Sellers and their agents should not make representations about such matters unless they are based on a reliable survey. In *Salahutdin v Valley of Cal., Inc.* (1994) 24 CA4th 555, 29 CR2d 463, the seller and listing agent represented that the property contained more than one acre, based on the location of a perimeter fence, without conducting a survey. The buyer's agent communicated these representations to the buyer. The buyer purchased the property with the intent to subdivide it. After the sale, the buyer discovered that the fence did not accurately mark the boundary and that the property was, in fact, less than one acre and thus could not be subdivided. The buyer's agent was found to have breached his fiduciary duty by communicating the seller's representations about the size of the lot to the buyer without disclosing that he had not independently verified its accuracy.

If the precise boundaries of the property are important to the buyer, then the purchase should be made contingent on confirmation of the boundaries by survey. Otherwise, as part of its due-diligence investigation, a buyer should inspect the property for evidence of possible boundary disputes, such as the absence of fencing, or fencing that is inconsistent with the shape of the parcel as depicted on a recorded map, and make appropriate inquiries of the seller. Similarly, the buyer should look for evidence of possible unrecorded easements or other interests (*e.g.,* a sewer pipe running across the property from an uphill property), particularly if the ability to use or develop a particular portion of the property is material to the buyer. In such case, a title insurance endorsement may be available to cover the issue of concern to the buyer. See §§6.82-6.85. For a discussion of buyer's due diligence, see §§6.71-6.77.

© The Regents of the University of California

§6.8 (2) Fixtures and Personal Property

A fixture is attached to the land by roots (*e.g.,* trees, vines, or shrubs), imbedded in the land (*e.g.,* walls), permanently resting on the land (*e.g.,* a building), or permanently attached to a building (such as by cement, plaster, nails, bolts, or screws). CC §660. Typically, fixtures are included in the sale of real property, whereas personal property is not. This is the default provision in the Residential Purchase Agreement and Joint Escrow Instructions, ¶8.B; see §6.24. Residential fixtures include electrical, mechanical, lighting, plumbing, and heating fixtures; ceiling fans, fireplace inserts, built-in appliances, window coverings, and attached flooring; and items such as cabinetry, shelving, or other furnishings that are nailed, bolted, screwed, or similarly attached to the dwelling. Fixtures do not include washer/dryers, refrigerators, and other appliances that can be unplugged and moved.

PRACTICE TIP: The Residential Purchase Agreement and Joint Escrow Instructions, ¶8.A (see §6.24) provides that items included or excluded in the Multiple Listing Service (MLS) listing and other advertising materials are not included in or excluded from the sale unless specified in the purchase contract. Thus, sellers need to specify in the purchase agreement any fixtures that are excluded from the sale, and buyers need to specify any personal property they wish to include in the sale.

© The Regents of the University of California

§6.9 b. "As Is" Clauses

There are no implied warranties as to quality or condition in the sale of real property except for newly constructed residential dwellings. *Pollard v Saxe & Yolles Dev. Co*. (1974) 12 C3d 374, 380, 115 CR 648 (implied warranty in new construction that structure is designed and constructed in reasonable, workmanlike manner); *East Hilton Drive Homeowners' Ass'n v Western Real Estate Exch., Inc.* (1982) 136 CA3d 630, 632, 186 CR 267. Rather, the buyer assumes the risk of the property's quality and condition absent express warranties, fraud, or misrepresentation by the seller. *Shapiro v Hu* (1986) 188 CA3d 324, 332, 233 CR 470.

"As is" clauses are often used to signal that the property is being sold in its present observable state and condition, without any implied warranties as to quality or condition. 188 CA3d at 332. It has been suggested that by so notifying the buyer, the seller raises a "red flag" that the property may not be "in perfect condition or of ideal quality." 188 CA3d at 333.

An "as is" clause relieves the seller of liability for defects in the property unless the seller, through fraud or misrepresentation, conceals material defects not otherwise known or observable to the buyer. 188 CA3d at 333. In other words, an "as is" clause does not relieve the seller of the common law and statutory duties of disclosure or liability for fraud. See CC §1102.1(a). See also *Wilson v Century 21 Great W. Realty* (1993) 15 CA4th 298, 304, 18 CR2d 779. For a discussion of statutory disclosure requirements, see §§6.34-6.70.

NOTE: The Residential Purchase Agreement and Joint Escrow Instructions (see §6.24) does not use the term "as is" but, in effect, incorporates the concept by providing in paragraphs 7.A and B that the property is being sold "in its PRESENT physical condition as of the date of Acceptance, subject to the buyer's investigation rights and the seller's duty to disclose known material facts and defects." For an example of an "as is" clause in a commercial purchase and sale agreement, see form 4.173-5.

© The Regents of the University of California

c. Liquidated Damages and Deposit Forfeiture

§6.10 (1) Owner-Occupied One to Four Units

Civil Code §§1675-1681 govern the validity and legal effect of a liquidated damages clause in a purchase agreement for the sale of a dwelling containing one to four residential units, if at the time of contracting the buyer intended to occupy one or more of the units as a personal residence. CC §1675(a). The validity of liquidated damages in all other contexts is governed by CC §1671. CC §1679. For a more detailed discussion of liquidated damages clauses, see §4.142 and California Real Property Remedies and Damages §§4.35-4.38 (2d ed Cal CEB 2002).

© The Regents of the University of California

§6.11 (a) Formal Requirements

For a liquidated damages provision in a residential purchase agreement (owner-occupied, one-to-four-unit property) to be valid:

(1) The provision must be signed or initialed by each party to the contract (CC §1677(a));

(2) If the provision is pre-printed, it must be in at least 10-point bold type or at least 8-point bold type in contrasting red print (CC §1677(b));

(3) If more than one payment is made, for each subsequent payment a separate liquidated damages provision must be executed, meeting requirements (1) and (2) above (CC §1678);

(4) The provision will be valid only to the extent of payment actually made at the time of the buyer's breach (CC §1675(c)); and

(5) The provision will be valid if the amount actually paid does not exceed 3 percent of the purchase price, unless the buyer establishes that the amount is unreasonable as liquidated damages. If the amount exceeds 3 percent, the provision will be invalid unless the party seeking to uphold it establishes it is reasonable as liquidated damages. CC §1675(d).

These rules do not preclude a seller, upon a buyer's default, from seeking specific performance in appropriate situations. See CC §1680.

© The Regents of the University of California

§6.12 (b) Reasonableness

A liquidated damages clause is valid if it was reasonable under the circumstances existing at the time the contract was made. See CC §§1671(b), 1675(e)(1). In the context of a one-to-four-unit residential sale, however, the criteria for reasonableness also include the price and other terms and circumstances of any sale of, or contract to sell, the same property that occurs within 6 months after the buyer's default. CC §1675(e)(2).

The Law Revision Commission Comments to CC §1675 provide guidance to courts on the factors they should consider in determining reasonableness. These include the cost of taxes, interest, and insurance during the period after the original contract to purchase the property was made and any additional broker's fees incurred as a result of the buyer's default. Other relevant factors include the relative equality of the parties' bargaining power, whether they were represented by lawyers when the contract was made, their anticipation that proof of actual damages would be costly or inconvenient, the difficulty of proving causation and foreseeability, and whether the liquidated damages provision is part of a form contract. See Law Revision Commission Comments to CC §1675.

© The Regents of the University of California

§6.13 (c) Deposit Forfeiture

The forfeiture of a buyer's deposit on default is not automatic. Although there are no published cases considering the requirement in CC §1675(e)(2) that a sale within 6 months of the buyer's default be considered in determining whether a liquidated damages provision is reasonable, given the overriding duty to mitigate damages, a seller should continue to actively market the property for sale during the 6-month period following default or risk a finding that the provision is unreasonable. Moreover, even if the amount of the deposit does not exceed 3 percent, a buyer might still argue unreasonableness based on CC §1675 if the facts and circumstances are supportive.

Ultimately, a buyer or seller could be liable to the other for failure to authorize the escrow holder to distribute the deposit. CC §1057.3(a). If, within 30 days following a written demand by one party for return of the deposit, the other party fails to execute documents authorizing the escrow holder to release funds, that party will be liable to the demanding party for the amount of the deposit not held to resolve a good faith dispute and treble damages of not less than $100 or more than $1000, plus reasonable attorney fees incurred to enforce this obligation. CC §1057.3(b). To prevail, the demanding party must prove that there was no good faith dispute as to the right to the deposit. CC §1057.3(c).

© The Regents of the University of California

§6.14 (2) Initial Sale of New Condominiums

Special rules apply to liquidated damages provisions in contracts for the initial sale of certain newly constructed attached residential condominium units. If the unit is located within a structure of ten or more residential units and the amount actually paid to the seller as liquidated damages on the buyer's default exceeds 3 percent of the purchase price, the seller must:

- Make reasonable efforts to mitigate damages (CC §1675(f)(1)(B));
- Perform an accounting of its costs and revenues allocable to the unit within 60 days after its subsequent sale (or 60 days after the seller enters into a contract with a buyer who has a loan commitment to purchase the unit at the same or higher price as the defaulting buyer) (CC §1675(f)(1)(A)); and
- Refund to the buyer, within 90 days after the final close of escrow of all sales and leases of units within the building, the greater of any amount retained by the seller in excess of 3 percent of the original sale price or the amount of the seller's actual losses according to the accounting. CC §1675(f)(1)(B), (2).

If, after the accounting, it is determined that the deposit retained by the seller does not exceed 3 percent, then the amount is considered valid unless the buyer establishes that it is unreasonable as liquidated damages. CC §1675(f)(3).

Beginning January 1, 2009, substantially similar accounting and refund requirements were imposed on the sale of attached residential condominium units located within a building that is over eight stories tall, contains 20 or more residential units, and is located in a high-density infill development, if the purchase price of the unit is more than $1 million. CC §1675(g). In such cases, if the liquidated damages paid exceed 6 percent of the unit's purchase price, the same accounting requirements as under CC §1675(f) apply, and the seller is required to refund the greater of any amount retained in excess of 6 percent of the original sale price or the amount of the seller's actual losses. CC §1675(g)(1)(A). When the retained amount does not exceed 6 percent, the liquidated damages provision is considered valid unless the buyer can establish that it is unreasonable under CC §1675(e). CC §1675(g)(3). See §6.12. If, however, the seller did not provide a specified statutory notice to the buyer regarding the deposit before execution of the purchase contract, the amount of liquidated damages the seller may recover will be limited to 3 percent of the purchase price, subject to the buyer establishing that the amount is unreasonable as liquidated damages or the seller establishing that a greater amount is reasonable as liquidated damages. CC §1675(g)(9). See §1675(c)-(d). Civil Code §1675(g) becomes inoperative on July 1, 2014 unless a later enacted statute, that becomes operative on or before January 1, 2015, extends it. CC §1675(h).

© The Regents of the University of California

§6.15 d. Alternative Dispute Resolution

The California arbitration law (CCP §§1280-1294.2) governs private arbitration in California unless the contract containing the arbitration clause involves interstate or foreign commerce, in which case the Federal Arbitration Act (9 USC §§1-16) preempts conflicting provisions of state law. See *Southland Corp. v Keating* (1984) 465 US 1, 12, 79 L Ed 2d 1, 104 S Ct 852. California arbitration statutes specify format and notice requirements for arbitration agreements in real estate contracts and expressly exclude certain types of claims from arbitration. See CCP §1298 and §§6.16-6.17. The relationship between these restrictive provisions and the broad arbitration mandate of the Federal Arbitration Act has been considered by California courts in several decisions, which have broadly construed the reach of the Federal Arbitration Act while taking care to enforce the intent of the contracting parties. See §6.18.

Additionally, parties may use statutory and common law contract arguments against the enforceability of arbitration agreements. See, *e.g., Thompson v Toll Dublin, LLC* (2008) 165 CA4th 1360, 81 CR3d 736 (arbitration provisions in preprinted documents that builder-seller required new home buyer to execute was unconscionable); *Marcus & Millichap Real Estate Inv. Brokerage Co. v Hock Inv. Co.* (1998) 68 CA4th 83, 80 CR2d 147 (lack of mutual agreement between the parties).

On alternative dispute resolution generally, see §4.150. See also California Real Property Remedies and Damages, chap 14 (2d ed Cal CEB 2002) and A Litigator's Guide to Effective Use of ADR in California (Cal CEB 2005). For a sample arbitration provision for use in a commercial real estate transaction, see form 4.177-5.

© The Regents of the University of California

(1) California Arbitration Provisions

§6.16 (a) Format and Notice Requirements

California law requires arbitration agreements in contracts for the sale of real property to satisfy certain format and notice requirements to be enforceable. CCP §1298. The arbitration provision must be entitled "ARBITRATION OF DISPUTES." CCP §1298(b). If the provision is included in a printed contract, it must be in at least 8-point bold type or contrasting red in at least 8-point type, or if the provision is in a typed contract, it must be in all capital letters. CCP §1298(b). Immediately following the arbitration provision there must be a statutorily specified Notice (in 10-point bold type or contrasting red 8-point bold type in printed contracts, or full capital letters in typed contracts), immediately followed by a space or line for the parties to initial or sign, evidencing their assent to the arbitration provision. CCP §1298(c). See the Residential Purchase Agreement and Joint Escrow Instructions, ¶17.B, in §6.24. The notice language itself does not constitute the arbitration agreement. *Villacreses v Molinari* (2005) 132 CA4th 1223, 1231, 34 CR3d 281.

© The Regents of the University of California

§6.17 (b) Exclusions From Arbitration

Under California law, an arbitration provision in a real estate purchase agreement cannot require arbitration of bodily injury or wrongful death claims, or certain construction or design defect claims. CCP §1298.7. See *Gravillis v Coldwell Banker Residential Brokerage Co.* (2006) 143 CA4th 761, 49 CR3d 531 (claim for emotional distress from nondisclosure of structural defects does not constitute "bodily injury" excluded from arbitration agreement).

NOTE: Paragraph 17.B of the Residential Purchase Agreement and Joint Escrow Instructions (see §6.24) excludes from its mediation and arbitration provisions foreclosure, unlawful detainer, mechanics' liens, small claims, probate, and bankruptcy actions.

© The Regents of the University of California

(2) Federal Arbitration Act

§6.18 (a) Preemption

Under the Federal Arbitration Act (FAA) (9 USC §§1-16), arbitration agreements in contracts "involving commerce" are enforceable subject only to state laws governing the validity, revocability, and enforceability of contracts in general (as opposed to state laws directed at arbitration agreements specifically). *Hedges v Carrigan* (2004) 117 CA4th 578, 583, 11 CR3d 787, citing *Doctor's Assocs., Inc. v Casarotto* (1996) 517 US 681, 686-687, 134 L Ed 2d 902, 116 S Ct 1652 (Montana statute conditioning arbitration agreements' enforceability on inclusion of special notice requirements directly conflicted with and was preempted by FAA as applied to agreement involving interstate commerce). Thus, the FAA preempts conflicting provisions of the California arbitration law in cases "involving commerce," which has been broadly construed. *Hedges,* 117 CA4th at 585. See also *Woolls v Superior Court* (2005) 127 CA4th 197, 212, 25 CR3d 426 (party asserting preemption must present facts showing transaction "involves commerce").

In *Hedges,* the court found that the sale of a single-family residence involved interstate commerce when the purchase was financed with an FHA home loan and the parties used transaction forms copyrighted by the National Association of Realtors®. Therefore, even though the parties' arbitration agreement failed to comply with the formal requirements of CCP §1298, the agreement was valid and enforceable under the FAA's broad arbitration mandate. 117 CA4th at 586. Similarly, in *Shepard v Edward Mackay Enters., Inc.* (2007) 148 CA4th 1092, 56 CR3d 326, the court found that the FAA preempted CCP §1298.7 when construction of the plaintiff's house involved receipt and use of building materials that were manufactured or produced outside California. It was not necessary that the dispute involve the materials from out of state as long as the number of building materials that came from out of state indicated more than a "trivial" impact on interstate commerce. 148 CA4th at 1101.

To the same effect is *Basura v U.S. Home Corp.* (2002) 98 CA4th 1205, 120 CR2d 328. There, relying on *Doctor's Assocs., Inc. v Casarotto* (1996) 517 US 681, 686-687, 134 L Ed 2d 902, 116 S Ct 1652, the court held that purchase contracts between a residential home builder and new home buyers involved interstate commerce when various structural components of the homes, appliances, and fixtures were manufactured outside of California; the builder contracted with out-of-state design professionals and contractors; the builder communicated with them and others by interstate mail and telephone; and the builder advertised throughout the country using interstate media. *Basura,* 98 CA4th at 1214.

© The Regents of the University of California

§6.18A (b) Application of State Contract Law

In *Marcus & Millichap Real Estate Inv. Brokerage Co. v Hock Inv. Co.* (1998) 68 CA4th 83, 80 CR2d 147, the court found that a lack of mutual agreement to arbitrate in the parties' contract is an issue of general California contract law that is not preempted by the Federal Arbitration Act (FAA) (9 USC §§1-16). In *Marcus & Millichap,* the purchase agreement contained an arbitration agreement and the notice language required by CCP §1298, followed by space for the seller and buyer to initial, but only one of the parties initialed. The court stated that, regardless of whether the FAA preempts CCP §1298, the language required by CCP §1298 was actually incorporated into the parties' contract, so the relevant question was whether the language of the contract reflected an agreement to arbitrate. 68 CA4th at 92.

Interpreting the language of the purchase agreement, the *Marcus & Millichap* court held that the contract contemplated that the arbitration agreement would be effective only if initialed by both parties. Because only one party initialed it, there was no agreement to arbitrate as a matter of California contract law. 68 CA4th at 92. In so holding, the court noted that if the parties' contract had not contained the language required by CCP §1298, the court might have found that the FAA preempted CCP §1298. 68 CA4th at 92.

© The Regents of the University of California

§6.19 e. Mediation and Attorney Fees

Most purchase agreement forms include a boilerplate provision for the award of attorney fees to the prevailing party in a dispute arising out of the agreement. As attorney fee awards can be substantial, these fee-shifting provisions, including any conditions or exceptions, should be carefully reviewed. For example, Paragraph 22 of the Residential Purchase Agreement and Joint Escrow Instructions in §6.24 provides that the prevailing party in an action, proceeding, or arbitration between the buyer and seller arising out of the purchase agreement is entitled to recover its reasonable attorney fees and costs, except as provided in ¶17.A. Paragraph 17.A requires the parties first to engage in mediation of any dispute (whether or not it is subject to arbitration) and provides that a party who files an action without first attempting to resolve it through mediation, or who refuses a request to mediate, forfeits any right to recover attorney fees, even if they would otherwise be available. Paragraph 17.A has been interpreted as a condition precedent to the recovery of attorney fees, barring recovery by a prevailing party who does not first attempt mediation. *Lange v Schilling* (2008) 163 CA4th 1412, 1417, 78 CR3d 356, citing *Johnson v Siegel* (2000) 84 CA4th 1087, 1101, 101 CR2d 412. Courts have repeatedly stated that ¶17.A "'means what it says and will be enforced.'" *Lange,* 163 CA4th at 1417, quoting *Frei v Davey* (2004) 124 CA4th 1506, 1508, 22 CR3d 429.

Given the strong policy favoring mediation "at the earliest possible time" and the clear and unambiguous language of ¶17.A, courts have rejected various excuses offered by parties for failing to mediate. *Lange,* 163 CA4th at 1417. In *Frei v Davey*, the buyers requested mediation after the sellers canceled the purchase agreement. When the sellers delayed in responding to the buyers' mediation request, the buyers filed a specific performance action. The buyers continued to propose mediation, but the sellers did not agree to mediate until nearly 1 year later, on the eve of trial. Although the mediation provision in the purchase agreement did not specify a response time to the mediation request, the court held that a reasonable time for performance must be allowed and that the sellers' initial delay and subsequent rejection of mediation were unreasonable. 124 CA4th at 1516. The court rejected the sellers' arguments that they had substantially complied with the mediation provision by engaging in settlement discussions and that their refusal to mediate should be excused because they perceived that mediation was unlikely to be successful. 124 CA4th at 1514. Acknowledging the value of mediation at various stages of a dispute, the court nevertheless stated that a 1-year delay in agreeing to mediate defeated the purpose of early-mediation provisions intended to minimize the cost of resolving a dispute. The court also rejected the sellers' argument that the buyers had negated the mediation requirement by filing the lawsuit in order to record a lis pendens against the property, noting that the arbitration provision in the purchase agreement permitted the filing of a lawsuit for that purpose. 124 CA4th at 1517. Thus, even though the sellers ultimately prevailed at trial, the court held that they were precluded from recovering attorney fees because of their refusal to mediate. 124 CA4th at 1520.

Similarly, in *Lange v Schilling,* the court declined to award a prevailing buyer attorney fees, rejecting all three of the buyer's reasons for failing to engage in mediation before filing his lawsuit. The court rejected the buyer's assertions that:

- He could not locate the sellers, noting that the buyer had hired an investigator to locate the sellers to serve the complaint and could have done the same to serve them with a mediation request. 163 CA4th at 1417;
- His offer to mediate made months after filing and serving the complaint was "substantial compliance" with ¶17.A, stating that doctrine did not apply because ¶17.A clearly mandates that a party attempt mediation before commencing litigation. 163 CA4th at 1418; and
- The sellers waived mediation because their counsel did not respond to a letter from the buyer's counsel unilaterally asserting such a waiver. 163 CA4th at 1418.

Despite courts' strict interpretation of ¶17.A, one court has upheld an award of attorney fees to a prevailing party that filed suit before participating in mediation under the unique circumstances of that case. In *Kahn v Chetcuti* (2002) 101 CA4th 61, 123 CR2d 606, while counsel were attempting to agree on a mediator, plaintiffs' counsel requested opposing counsel to sign a tolling agreement because the limitations period on plaintiffs' claims was about to run, but opposing counsel refused to do so. Plaintiffs then filed the lawsuit solely to preserve their legal rights. Thereafter, the parties engaged in mediation before proceeding to arbitration. 101 CA4th at 67.

These cases demonstrate that courts will strictly interpret the condition precedent set forth in ¶17.A. However, in certain limited circumstances, the condition may be excused when the pre-mediation filing is necessary to preserve a legal right.

© The Regents of the University of California

§6.20 f. Contract Contingencies

Typically, a residential purchase agreement contains several contingencies that must be removed within specified time periods after acceptance or one or both of the parties may cancel the purchase agreement. The most common contingencies pertain to financing (the buyer must be approved for a loan in the required amount with certain specified terms); appraisal (the property must appraise at no less than the specified purchase price); buyer's investigations (buyer must approve inspection reports, seller disclosures and documents, and any other investigations and inquiries buyer chooses to make); title (buyer must approve seller's title and accept liens and encumbrances on the property that will survive close of escrow); and sale of another property owned by the buyer (performance not required unless buyer sells a specified property). Form purchase agreements generally require the buyer and seller to specify time periods within which the buyer must satisfy or release each contingency. See, *e.g.,* the CAR Residential Purchase Agreement and Joint Escrow Instructions, ¶14, in §6.24. For an example of a custom provision in a commercial purchase and sale agreement, see §4.171.

© The Regents of the University of California

§6.21 (1) Conditions Precedent

A contract contingency is, as a matter of contract law, a condition precedent. It is an act that must be performed, or an uncertain event that must happen, before a contractual right accrues or a contractual duty arises. *Realmuto v Gagnard* (2003) 110 CA4th 193, 199, 1 CR3d 569. See also CC §1436. The party whose performance is subject to a condition precedent must act in good faith and diligently to satisfy or "remove" the condition. *Jacobs v Freeman* (1980) 104 CA3d 177, 188, 163 CR 680 (officers of corporate seller that conditioned sale on approval of its board breached implied duty of good faith and fair dealing by failing to submit transaction documents to its board); *Abrams v Motter* (1970) 3 CA3d 828, 837, 83 CR 855 (buyer failed to act diligently in obtaining loan). This obligation derives from the covenant of good faith and fair dealing implied in every contract, which prohibits a contracting party from doing anything that prevents the other party from receiving the benefits of the agreement. *Bleecher v Conte* (1981) 29 C3d 345, 352, 213 CR 852. See also *Peak-Las Positas Partners v Bollag* (2009) 172 CA4th 101, 106, 90 CR3d 775 (seller's refusal to extend escrow was in bad faith when developer-buyer had already paid nearly all of purchase price into escrow and spent additional $5 million in project costs, and timing of transaction was not issue for seller). For a discussion of the duty of good faith and fair dealing, see Drafting Business Contracts: Principles, Techniques & Forms §9.23 (Cal CEB 1994).

The contingencies commonly included in residential agreements are referred to as "satisfaction clauses" because the buyer's obligation to perform is conditioned on his or her approval or satisfaction as to specified matters. See *Bleecher v Conte, supra* (buyer's performance contingent on approval of title report, plat map, and soil, zoning, and engineering reports); *Converse v Fong* (1984) 159 CA3d 86, 90, 205 CR 242 (buyer's obligation to perform conditioned on approval of termite and roof inspection reports). When a party's satisfaction as to a particular matter is a condition for the party's performance, the party has an implied duty to exercise its judgment in good faith and proceed diligently. *Bleecher,* 29 C3d at 352; *Converse,* 159 CA3d at 90. Two standards apply to this duty, depending on the nature of the condition involved. When the condition involves something that can be objectively measured or assessed, such as "commercial value or quality, operative fitness, or mechanical utility," a "reasonable person" standard applies and dissatisfaction cannot be claimed arbitrarily, unreasonably, or capriciously. *Mattei v Hopper* (1958) 51 C2d 119, 123, 330 P2d 625. However, when the condition involves matters of "fancy, taste, or judgment," the inquiry is limited to whether the person acted in good faith in disapproving the matter. *Mattei v Hopper, supra*.

© The Regents of the University of California

§6.22 (2) Contingency Removal

When a condition precedent is not timely performed, either party may terminate the purchase agreement. See *Consolidated World Invs., Inc. v Lido Preferred Ltd.* (1992) 9 CA4th 373, 380, 11 CR2d 524. Contracting parties are free to specify the time and manner in which a contingency must be removed and the consequences of a failure to do so. Paragraph 14 of the Residential Purchase Agreement and Joint Escrow Instructions in §6.24 provides a contingency-removal procedure that, although somewhat complex, ensures a clear record of the parties' intentions with respect to contractual conditions.

Under that procedure, the parties agree to the length of each contingency period (unless the parties expressly agree to waive any of the contingencies). During the contingency period, the buyer may request the seller to make certain repairs or take other action regarding the property, and on completion may remove the applicable contingency. The parties agree, however, that the seller has no obligation to agree or respond to the buyer's requests. The buyer further agrees either to remove the contingency in writing or to cancel the purchase agreement by the end of each contingency period. See ¶14.B(2)-(3) of the form in §6.24. As to certain matters that are within the control of the seller or third parties (such as condominium disclosures and documents), the parties agree that the contingency period will be a specified time period after the buyer receives the relevant materials for review. See ¶14.B(3). If the buyer fails to timely remove a contingency, the seller has the right to cancel the agreement, without penalty to the buyer, after first giving the buyer a Notice to Buyer to Perform. See §6.28. This notice declares the buyer's failure to perform and demands performance within a time-frame agreed to in the contract (24 hours is the default provision). See ¶14.C(1), (4). If a contingency period expires without removal of the contingency, the buyer retains the right to make requests of the seller, remove the contingency, or cancel the agreement up until the time the seller cancels in writing (after first giving the required notice). When the buyer has removed all contingencies (irrespective of timeliness), the seller no longer has the right to cancel the agreement. See ¶14.C(2).

© The Regents of the University of California

§6.23 g. Allocations, Prorations, and Cost Estimates

The purchase agreement should provide for the allocation of one-time (nonrecurring) transaction costs between the buyer and seller. Recurring costs associated with the property should also be prorated as of the date escrow closes.

Transaction costs include escrow charges, title insurance (covering buyer and lender), transfer taxes (county and city, if any), inspections and reports (including a pest inspection and the natural hazard disclosure report), and the cost to comply with any local governmental requirements. See the Residential Purchase Agreement and Joint Escrow Instructions, ¶4, in §6.24 regarding allocation of costs. All such costs are negotiable between the buyer and seller, but there are customary allocations that vary by county or region, which will be known by local real estate licensees and escrow agents.

EXAMPLE: In Alameda County, it is customary for the buyer to pay escrow and title insurance fees; for the seller to pay the county transfer tax; and for the buyer and seller to split any city transfer tax equally.

Prorated costs include real property taxes, homeowners' association dues, and rents. These costs are prorated by the escrow holder as of the close of escrow, generally based on a 30-day month. See the Residential Purchase Agreement and Joint Escrow Instructions, ¶18, regarding prorations. The escrow holder will prorate mortgage interest and pay off the seller's loan as of the close of escrow and charge the buyer for interest on its new purchase money loan as of the date the loan is funded.

NOTE: These and other transaction costs should be estimated and disclosed to the buyer by his or her real estate agent in conjunction with preparing the buyer's offer.

The Real Estate Settlement Procedures Act of 1974 (RESPA) (12 USC §§2601-2617) requires disclosure of closing (settlement) costs at various stages of a transaction involving a "federally related mortgage loan." 12 USC §§2602(1), 2603. In 2008, the Department of Housing and Urban Development (HUD) promulgated new RESPA rules designed to require more timely and effective disclosure of settlement costs in order to make the mortgage financing process clearer and less costly to consumers. See 73 Fed Reg 68204 (2008). Effective January 1, 2010, a lender or mortgage broker will be required to deliver or mail to the borrower, within 3 days of receiving a loan application or information sufficient to complete an application, a good faith estimate (GFE) of the closing costs the borrower is likely to pay and related information about loan terms and fees. The GFE must be made on a new standardized form created by HUD to be known as Form HUD-GFE. See 24 CFR §§3500.1(b)(2), 3500.7; for copy of form see App X. In addition, before close of escrow, the settlement agent (usually an escrow agent) must provide both the buyer and seller with an estimate of closing costs and, at closing, a final Settlement Statement, prepared on the HUD-1 form (for form see App Y), which fully accounts for the buyer's and seller's sides of the transaction. See 24 CFR §§3500.8. On these new forms, see §15.95.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/6 Residential Purchase and Sale Transactions/ B. CAR Residential Property Forms/§6.24 1. Form: California Residential Purchase Agreement and Joint Escrow Instructions (CAR Form RPA-CA)

B. CAR Residential Property Forms

§6.24 1. Form: California Residential Purchase Agreement and Joint Escrow Instructions (CAR Form RPA-CA)



CALIFORNIA ASSOCIATION OF REALTORS ®

CALIFORNIA RESIDENTIAL PURCHASE AGREEMENT AND JOINT ESCROW INSTRUCTIONS

For Use With Single Family Residential Property — Attached or Detached

(C.A.R. Form RPA-CA, Revised 11/07)

Date _____, at _____, California.

1. **OFFER:**
   A. **THIS IS AN OFFER FROM** _____ ("Buyer").
   B. **THE REAL PROPERTY TO BE ACQUIRED** is described as _____, Assessor's Parcel No. _____, situated in _____, County of _____, California, ("Property").
   C. **THE PURCHASE PRICE** offered is _____ Dollars $ _____.
   D. **CLOSE OF ESCROW** shall occur on _____ (date)(or ☐ _____ **Days** After Acceptance).
2. **FINANCE TERMS:** Obtaining the loans below is **a contingency** of this Agreement unless: **(i)** either 2K or 2L is checked below; or **(ii)** otherwise agreed in writing. Buyer shall act diligently and in good faith to obtain the designated loans. Obtaining deposit, down payment and closing costs **is not a contingency**. Buyer represents that funds will be good when deposited with Escrow Holder.
   A. **INITIAL DEPOSIT:** Buyer has given a deposit in the amount of ..... $ _____ to the agent submitting the offer (or to ☐ _____), by personal check (or ☐ _____), made payable to _____, which shall be held uncashed until Acceptance and then deposited within **3** business days after Acceptance (or ☐ _____), with Escrow Holder, (or ☐ into Broker's trust account).
   B. **INCREASED DEPOSIT:** Buyer shall deposit with Escrow Holder an increased deposit in the amount of ... $ _____ within ____ **Days** After Acceptance, or ☐ _____.
   C. **FIRST LOAN IN THE AMOUNT OF** ..... $ _____
      (1) NEW First Deed of Trust in favor of lender, encumbering the Property, securing a note payable at maximum interest of _____% fixed rate, or _____% initial adjustable rate with a maximum interest rate of _____%, balance due in _____ years, amortized over _____ years. Buyer shall pay loan fees/points not to exceed _____. (These terms apply whether the designated loan is conventional, FHA or VA.)
      (2) ☐ FHA ☐ VA: (The following terms only apply to the FHA or VA loan that is checked.) Seller shall pay _____% discount points. Seller shall pay other fees not allowed to be paid by Buyer, ☐ not to exceed $_____. Seller shall pay the cost of lender required Repairs (including those for wood destroying pest) not otherwise provided for in this Agreement, ☐ not to exceed $ _____. (Actual loan amount may increase if mortgage insurance premiums, funding fees or closing costs are financed.)
   D. **ADDITIONAL FINANCING TERMS:** ☐ Seller financing (C.A.R. Form SFA); ☐ secondary financing (C.A.R. Form PAA, paragraph 4A); ☐ assumed financing (C.A.R. Form PAA, paragraph 4B) ..... $ _____
   E. **BALANCE OF PURCHASE PRICE** (not including costs of obtaining loans and other closing costs) in the amount of ... $ _____ to be deposited with Escrow Holder within sufficient time to close escrow.
   F. **PURCHASE PRICE (TOTAL):** ..... $ _____
   G. **LOAN APPLICATIONS:** Within **7 (or** ☐ _____**)** **Days** After Acceptance, Buyer shall provide Seller a letter from lender or mortgage loan broker stating that, based on a review of Buyer's written application and credit report, Buyer is prequalified or preapproved for the NEW loan specified in 2C above.
   H. **VERIFICATION OF DOWN PAYMENT AND CLOSING COSTS:** Buyer (or Buyer's lender or loan broker pursuant to 2G) shall, within **7 (or** ☐ _____**)** **Days** After Acceptance, provide Seller written verification of Buyer's down payment and closing costs.
   I. **LOAN CONTINGENCY REMOVAL: (i)** Within **17 (or** ☐ _____**)** **Days** After Acceptance, Buyer shall, as specified in paragraph 14, remove the loan contingency or cancel this Agreement; **OR (ii)** (if checked) ☐ the loan contingency shall remain in effect until the designated loans are funded.
   J. **APPRAISAL CONTINGENCY AND REMOVAL:** This Agreement is (**OR**, if checked, ☐ is NOT) contingent upon the Property appraising at no less than the specified purchase price. If there is a loan contingency, at the time the loan contingency is removed (or, if checked, ☐ within **17 (or** ____**)** **Days** After Acceptance), Buyer shall, as specified in paragraph 14B(3), remove the appraisal contingency or cancel this Agreement. If there is no loan contingency, Buyer shall, as specified in paragraph 14B(3), remove the appraisal contingency within **17 (or** ____**)** **Days** After Acceptance.
   K. ☐ **NO LOAN CONTINGENCY** (If checked): Obtaining any loan in paragraphs 2C, 2D or elsewhere in this Agreement is NOT a contingency of this Agreement. If Buyer does not obtain the loan and as a result Buyer does not purchase the Property, Seller may be entitled to Buyer's deposit or other legal remedies.
   L. ☐ **ALL CASH OFFER** (If checked): No loan is needed to purchase the Property. Buyer shall, within **7 (or** ☐ _____**)** **Days** After Acceptance, provide Seller written verification of sufficient funds to close this transaction.
3. **CLOSING AND OCCUPANCY:**
   A. Buyer intends (or ☐ does not intend) to occupy the Property as Buyer's primary residence.
   B. **Seller-occupied or vacant property:** Occupancy shall be delivered to Buyer at _____ AM/PM, ☐ on the date of Close Of Escrow; ☐ on _____; or ☐ no later than _____ **Days** After Close Of Escrow. (C.A.R. Form PAA, paragraph 2.) If transfer of title and occupancy do not occur at the same time, Buyer and Seller are advised to: **(i)** enter into a written occupancy agreement; and **(ii)** consult with their insurance and legal advisors.

The copyright laws of the United States (Title 17 U.S. Code) forbid the unauthorized reproduction of this form, or any portion thereof, by photocopy machine or any other means, including facsimile or computerized formats. Copyright © 1991-2007, CALIFORNIA ASSOCIATION OF REALTORS®, INC. ALL RIGHTS RESERVED.

Buyer's Initials (_____)(_____)
Seller's Initials (_____)(_____)

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

Print

C. **Tenant-occupied property: (i) Property shall be vacant** at least 5 (or ☐ _____) **Days** Prior to Close Of Escrow, unless otherwise agreed in writing. **Note to Seller: If you are unable to deliver Property vacant in accordance with rent control and other applicable Law, you may be in breach of this Agreement.**

OR (ii) (if checked) ☐ **Tenant to remain in possession.** The attached addendum is incorporated into this Agreement (C.A.R. Form PAA, paragraph 3.);

OR (iii) (if checked) ☐ **This Agreement is contingent** upon Buyer and Seller entering into a written agreement regarding occupancy of the Property within the time specified in paragraph 14B(1). If no written agreement is reached within this time, either Buyer or Seller may cancel this Agreement in writing.

D. At Close Of Escrow, Seller assigns to Buyer any assignable warranty rights for items included in the sale and shall provide any available Copies of such warranties. Brokers cannot and will not determine the assignability of any warranties.

E. At Close Of Escrow, unless otherwise agreed in writing, Seller shall provide keys and/or means to operate all locks, mailboxes, security systems, alarms and garage door openers. If Property is a condominium or located in a common interest subdivision, Buyer may be required to pay a deposit to the Homeowners' Association ("HOA") to obtain keys to accessible HOA facilities.

4. **ALLOCATION OF COSTS** (If checked): Unless otherwise specified here, this paragraph only determines who is to pay for the report, inspection, test or service mentioned. If not specified here or elsewhere in this Agreement, the determination of who is to pay for any work recommended or identified by any such report, inspection, test or service shall be by the method specified in paragraph 14B(2).

A. **WOOD DESTROYING PEST INSPECTION:**

(1) ☐ Buyer ☐ Seller shall pay for an inspection and report for wood destroying pests and organisms ("Report") which shall be prepared by _____, a registered structural pest control company. The Report shall cover the accessible areas of the main building and attached structures and, if checked: ☐ detached garages and carports, ☐ detached decks, ☐ the following other structures or areas _____. The Report shall not include roof coverings. If Property is a condominium or located in a common interest subdivision, the Report shall include only the separate interest and any exclusive-use areas being transferred and shall not include common areas, unless otherwise agreed. Water tests of shower pans on upper level units may not be performed without consent of the owners of property below the shower.

OR (2) ☐ **(If checked)** The attached addendum (C.A.R. Form WPA) regarding wood destroying pest inspection and allocation of cost is incorporated into this Agreement.

B. **OTHER INSPECTIONS AND REPORTS:**

(1) ☐ Buyer ☐ Seller shall pay to have septic or private sewage disposal systems inspected _____.
(2) ☐ Buyer ☐ Seller shall pay to have domestic wells tested for water potability and productivity _____.
(3) ☐ Buyer ☐ Seller shall pay for a natural hazard zone disclosure report prepared by _____.
(4) ☐ Buyer ☐ Seller shall pay for the following inspection or report _____.
(5) ☐ Buyer ☐ Seller shall pay for the following inspection or report _____.

C. **GOVERNMENT REQUIREMENTS AND RETROFIT:**

(1) ☐ Buyer ☐ Seller shall pay for smoke detector installation and/or water heater bracing, if required by Law. Prior to Close Of Escrow, Seller shall provide Buyer a written statement of compliance in accordance with state and local Law, unless exempt.
(2) ☐ Buyer ☐ Seller shall pay the cost of compliance with any other minimum mandatory government retrofit standards, inspections and reports if required as a condition of closing escrow under any Law. _____.

D. **ESCROW AND TITLE:**

(1) ☐ Buyer ☐ Seller shall pay escrow fee _____.
Escrow Holder shall be _____.
(2) ☐ Buyer ☐ Seller shall pay for **owner's** title insurance policy specified in paragraph 12E _____.
Owner's title policy to be issued by _____.
(Buyer shall pay for any title insurance policy insuring Buyer's **lender**, unless otherwise agreed in writing.)

E. **OTHER COSTS:**

(1) ☐ Buyer ☐ Seller shall pay County transfer tax or transfer fee _____.
(2) ☐ Buyer ☐ Seller shall pay City transfer tax or transfer fee _____.
(3) ☐ Buyer ☐ Seller shall pay HOA transfer fee _____.
(4) ☐ Buyer ☐ Seller shall pay HOA document preparation fees _____.
(5) ☐ Buyer ☐ Seller shall pay the cost, not to exceed $ _____, of a one-year home warranty plan, issued by _____,
with the following optional coverage: _____.
(6) ☐ Buyer ☐ Seller shall pay for _____.
(7) ☐ Buyer ☐ Seller shall pay for _____.

5. **STATUTORY DISCLOSURES (INCLUDING LEAD-BASED PAINT HAZARD DISCLOSURES) AND CANCELLATION RIGHTS:**

A. **(1)** Seller shall, within the time specified in paragraph 14A, deliver to Buyer, if required by Law: **(i)** Federal Lead-Based Paint Disclosures and pamphlet ("Lead Disclosures"); and **(ii)** disclosures or notices required by sections 1102 et. seq. and 1103 et. seq. of the California Civil Code ("Statutory Disclosures"). Statutory Disclosures include, but are not limited to, a Real Estate Transfer Disclosure Statement ("TDS"), Natural Hazard Disclosure Statement ("NHD"), notice or actual knowledge of release of illegal controlled substance, notice of special tax and/or assessments (or, if allowed, substantially equivalent notice regarding the Mello-Roos Community Facilities Act and Improvement Bond Act of 1915) and, if Seller has actual knowledge, of industrial use and military ordinance location disclosure (C.A.R. Form SSD).

(2) Buyer shall, within the time specified in paragraph 14B(1), return Signed Copies of the Statutory and Lead Disclosures to Seller.

(3) In the event Seller, prior to Close Of Escrow, becomes aware of adverse conditions materially affecting the Property, or any material inaccuracy in disclosures, information or representations previously provided to Buyer of which Buyer is otherwise unaware, Seller shall promptly provide a subsequent or amended disclosure or notice, in writing, covering those items. **However, a subsequent or amended disclosure shall not be required for conditions and material inaccuracies disclosed in reports ordered and paid for by Buyer.**

Buyer's Initials (_____)(_____)
Seller's Initials (_____)(_____)

Copyright © 1991-2007, CALIFORNIA ASSOCIATION OF REALTORS®, INC.

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

Print

(4) If any disclosure or notice specified in 5A(1), or subsequent or amended disclosure or notice is delivered to Buyer after the offer is Signed, Buyer shall have the right to cancel this Agreement within **3 Days** After delivery in person, or **5 Days** After delivery by deposit in the mail, by giving written notice of cancellation to Seller or Seller's agent. (Lead Disclosures sent by mail must be sent certified mail or better.)

(5) Note to Buyer and Seller: Waiver of Statutory and Lead Disclosures is prohibited by Law.

B. NATURAL AND ENVIRONMENTAL HAZARDS: Within the time specified in paragraph 14A, Seller shall, if required by Law: **(i)** deliver to Buyer earthquake guides (and questionnaire) and environmental hazards booklet; **(ii)** even if exempt from the obligation to provide a NHD, disclose if the Property is located in a Special Flood Hazard Area; Potential Flooding (Inundation) Area; Very High Fire Hazard Zone; State Fire Responsibility Area; Earthquake Fault Zone; Seismic Hazard Zone; and **(iii)** disclose any other zone as required by Law and provide any other information required for those zones.

C. MEGAN'S LAW DATABASE DISCLOSURE: Notice: Pursuant to Section 290.46 of the Penal Code, information about specified registered sex offenders is made available to the public via an Internet Web site maintained by the Department of Justice at www.meganslaw.ca.gov. Depending on an offender's criminal history, this information will include either the address at which the offender resides or the community of residence and ZIP Code in which he or she resides. (Neither Seller nor Brokers are required to check this website. If Buyer wants further information, Broker recommends that Buyer obtain information from this website during Buyer's inspection contingency period. Brokers do not have expertise in this area.)

6. CONDOMINIUM/PLANNED UNIT DEVELOPMENT DISCLOSURES:

A. SELLER HAS: 7 (or ☐ _____) Days After Acceptance to disclose to Buyer whether the Property is a condominium, or is located in a planned unit development or other common interest subdivision (C.A.R. Form SSD).

B. If the Property is a condominium or is located in a planned unit development or other common interest subdivision, Seller has **3 (or ☐ _____) Days** After Acceptance to request from the HOA (C.A.R. Form HOA): **(i)** Copies of any documents required by Law; **(ii)** disclosure of any pending or anticipated claim or litigation by or against the HOA; **(iii)** a statement containing the location and number of designated parking and storage spaces; **(iv)** Copies of the most recent 12 months of HOA minutes for regular and special meetings; and **(v)** the names and contact information of all HOAs governing the Property (collectively, "CI Disclosures"). Seller shall itemize and deliver to Buyer all CI Disclosures received from the HOA and any CI Disclosures in Seller's possession. Buyer's approval of CI Disclosures is a contingency of this Agreement as specified in paragraph 14B(3).

7. CONDITIONS AFFECTING PROPERTY:

A. Unless otherwise agreed: **(i) the Property is sold (a) in its PRESENT physical condition as of the date of Acceptance and (b) subject to Buyer's Investigation rights; (ii)** the Property, including pool, spa, landscaping and grounds, is to be maintained in substantially the same condition as on the date of Acceptance; and **(iii)** all debris and personal property not included in the sale shall be removed by Close Of Escrow.

B. SELLER SHALL, within the time specified in paragraph 14A, DISCLOSE KNOWN MATERIAL FACTS AND DEFECTS affecting the Property, including known insurance claims within the past five years, AND MAKE OTHER DISCLOSURES REQUIRED BY LAW (C.A.R. Form SSD).

C. NOTE TO BUYER: You are strongly advised to conduct investigations of the entire Property in order to determine its present condition since Seller may not be aware of all defects affecting the Property or other factors that you consider important. Property improvements may not be built according to code, in compliance with current Law, or have had permits issued.

D. NOTE TO SELLER: Buyer has the right to inspect the Property and, as specified in paragraph 14B, based upon information discovered in those inspections: (i) cancel this Agreement; or (ii) request that you make Repairs or take other action.

8. ITEMS INCLUDED AND EXCLUDED:

A. NOTE TO BUYER AND SELLER: Items listed as included or excluded in the MLS, flyers or marketing materials are **not** included in the purchase price or excluded from the sale unless specified in 8B or C.

B. ITEMS INCLUDED IN SALE:

(1) All EXISTING fixtures and fittings that are attached to the Property;

(2) Existing electrical, mechanical, lighting, plumbing and heating fixtures, ceiling fans, fireplace inserts, gas logs and grates, solar systems, built-in appliances, window and door screens, awnings, shutters, window coverings, attached floor coverings, television antennas, satellite dishes, private integrated telephone systems, air coolers/conditioners, pool/spa equipment, garage door openers/remote controls, mailbox, in-ground landscaping, trees/shrubs, water softeners, water purifiers, security systems/alarms; and

(3) The following items: _____
_____.

(4) Seller represents that all items included in the purchase price, unless otherwise specified, are owned by Seller.

(5) All items included shall be transferred free of liens and without Seller warranty.

C. ITEMS EXCLUDED FROM SALE: _____
_____.

9. BUYER'S INVESTIGATION OF PROPERTY AND MATTERS AFFECTING PROPERTY:

A. Buyer's acceptance of the condition of, and any other matter affecting the Property, is a contingency of this Agreement as specified in this paragraph and paragraph 14B. Within the time specified in paragraph 14B(1), Buyer shall have the right, at Buyer's expense unless otherwise agreed, to conduct inspections, investigations, tests, surveys and other studies ("Buyer Investigations"), including, but not limited to, the right to: **(i)** inspect for lead-based paint and other lead-based paint hazards; **(ii)** inspect for wood destroying pests and organisms; **(iii)** review the registered sex offender database; **(iv)** confirm the insurability of Buyer and the Property; and **(v)** satisfy Buyer as to any matter specified in the attached Buyer's Inspection Advisory (C.A.R. Form BIA). Without Seller's prior written consent, Buyer shall neither make nor cause to be made: **(i)** invasive or destructive Buyer Investigations; or **(ii)** inspections by any governmental building or zoning inspector or government employee, unless required by Law.

B. Buyer shall complete Buyer Investigations and, as specified in paragraph 14B, remove the contingency or cancel this Agreement. Buyer shall give Seller, at no cost, complete Copies of all Buyer Investigation reports obtained by Buyer. Seller shall make the Property available for all Buyer Investigations. Seller shall have water, gas, electricity and all operable pilot lights on for Buyer's Investigations and through the date possession is made available to Buyer.

Copyright © 1991-2007, CALIFORNIA ASSOCIATION OF REALTORS®, INC.

Print

10. **REPAIRS:** Repairs shall be completed prior to final verification of condition unless otherwise agreed in writing. Repairs to be performed at Seller's expense may be performed by Seller or through others, provided that the work complies with applicable Law, including governmental permit, inspection and approval requirements. Repairs shall be performed in a good, skillful manner with materials of quality and appearance comparable to existing materials. It is understood that exact restoration of appearance or cosmetic items following all Repairs may not be possible. Seller shall: **(i)** obtain receipts for Repairs performed by others; **(ii)** prepare a written statement indicating the Repairs performed by Seller and the date of such Repairs; and **(iii)** provide Copies of receipts and statements to Buyer prior to final verification of condition.
11. **BUYER INDEMNITY AND SELLER PROTECTION FOR ENTRY UPON PROPERTY:** Buyer shall: **(i)** keep the Property free and clear of liens; **(ii)** repair all damage arising from Buyer Investigations; and **(iii)** indemnify and hold Seller harmless from all resulting liability, claims, demands, damages and costs. Buyer shall carry, or Buyer shall require anyone acting on Buyer's behalf to carry, policies of liability, workers' compensation and other applicable insurance, defending and protecting Seller from liability for any injuries to persons or property occurring during any Buyer Investigations or work done on the Property at Buyer's direction prior to Close Of Escrow. Seller is advised that certain protections may be afforded Seller by recording a "Notice of Non-responsibility" (C.A.R. Form NNR) for Buyer Investigations and work done on the Property at Buyer's direction. Buyer's obligations under this paragraph shall survive the termination of this Agreement.
12. **TITLE AND VESTING:**
    A. Within the time specified in paragraph 14, Buyer shall be provided a current preliminary (title) report, which is only an offer by the title insurer to issue a policy of title insurance and may not contain every item affecting title. Buyer's review of the preliminary report and any other matters which may affect title are a contingency of this Agreement as specified in paragraph 14B.
    B. Title is taken in its present condition subject to all encumbrances, easements, covenants, conditions, restrictions, rights and other matters, whether of record or not, as of the date of Acceptance except: **(i)** monetary liens of record unless Buyer is assuming those obligations or taking the Property subject to those obligations; and **(ii)** those matters which Seller has agreed to remove in writing.
    C. Within the time specified in paragraph 14A, Seller has a duty to disclose to Buyer all matters known to Seller affecting title, whether of record or not.
    D. At Close Of Escrow, Buyer shall receive a grant deed conveying title (or, for stock cooperative or long-term lease, an assignment of stock certificate or of Seller's leasehold interest), including oil, mineral and water rights if currently owned by Seller. Title shall vest as designated in Buyer's supplemental escrow instructions. THE MANNER OF TAKING TITLE MAY HAVE SIGNIFICANT LEGAL AND TAX CONSEQUENCES. CONSULT AN APPROPRIATE PROFESSIONAL.
    E. Buyer shall receive a CLTA/ALTA Homeowner's Policy of Title Insurance. A title company, at Buyer's request, can provide information about the availability, desirability, coverage, and cost of various title insurance coverages and endorsements. If Buyer desires title coverage other than that required by this paragraph, Buyer shall instruct Escrow Holder in writing and pay any increase in cost.
13. **SALE OF BUYER'S PROPERTY:**
    A. This Agreement is NOT contingent upon the sale of any property owned by Buyer.
    OR B. ☐ (If checked): The attached addendum (C.A.R. Form COP) regarding the contingency for the sale of property owned by Buyer is incorporated into this Agreement.
14. **TIME PERIODS; REMOVAL OF CONTINGENCIES; CANCELLATION RIGHTS: The following time periods may only be extended, altered, modified or changed by mutual written agreement. Any removal of contingencies or cancellation under this paragraph must be in writing (C.A.R. Form CR).**
    A. SELLER HAS: 7 (or ☐ _____) Days After Acceptance to deliver to Buyer all reports, disclosures and information for which Seller is responsible under paragraphs 4, 5A and B, 6A, 7B and 12.
    B. (1) BUYER HAS: 17 (or ☐ _____) Days After Acceptance, unless otherwise agreed in writing, to:
    (i) complete all Buyer Investigations; approve all disclosures, reports and other applicable information, which Buyer receives from Seller; and approve all matters affecting the Property (including lead-based paint and lead-based paint hazards as well as other information specified in paragraph 5 and insurability of Buyer and the Property); and
    (ii) return to Seller Signed Copies of Statutory and Lead Disclosures delivered by Seller in accordance with paragraph 5A.
    (2) Within the time specified in 14B(1), Buyer may request that Seller make repairs or take any other action regarding the Property (C.A.R. Form RR). Seller has no obligation to agree to or respond to Buyer's requests.
    (3) By the end of the time specified in 14B(1) (or 2I for loan contingency or 2J for appraisal contingency), Buyer shall, in writing, remove the applicable contingency (C.A.R. Form CR) or cancel this Agreement. However, if **(i)** government-mandated inspections/reports required as a condition of closing; or **(ii)** Common Interest Disclosures pursuant to paragraph 6B are not made within the time specified in 14A, then Buyer has **5 (or ☐ _____) Days** After receipt of any such items, or the time specified in 14B(1), whichever is later, to remove the applicable contingency or cancel this Agreement in writing.
    C. CONTINUATION OF CONTINGENCY OR CONTRACTUAL OBLIGATION; SELLER RIGHT TO CANCEL:
    (1) Seller right to Cancel; Buyer Contingencies: Seller, after first giving Buyer a Notice to Buyer to Perform (as specified below), may cancel this Agreement in writing and authorize return of Buyer's deposit if, by the time specified in this Agreement, Buyer does not remove in writing the applicable contingency or cancel this Agreement. Once all contingencies have been removed, failure of either Buyer or Seller to close escrow on time may be a breach of this Agreement.
    (2) Continuation of Contingency: Even after the expiration of the time specified in 14B, Buyer retains the right to make requests to Seller, remove in writing the applicable contingency or cancel this Agreement until Seller cancels pursuant to 14C(1). Once Seller receives Buyer's written removal of all contingencies, Seller may not cancel this Agreement pursuant to 14C(1).
    (3) Seller right to Cancel; Buyer Contract Obligations: Seller, after first giving Buyer a Notice to Buyer to Perform (as specified below), may cancel this Agreement in writing and authorize return of Buyer's deposit for any of the following reasons: **(i)** if Buyer fails to deposit funds as required by 2A or 2B; **(ii)** if the funds deposited pursuant to 2A or 2B are not good when deposited; **(iii)** if Buyer fails to provide a letter as required by 2G; **(iv)** if Buyer fails to provide verification as required by 2H or 2L; **(v)** if Seller reasonably disapproves of the verification provided by 2H or 2L; **(vi)** if Buyer fails to return Statutory and Lead Disclosures as required by paragraph 5A(2); or **(vii)** if Buyer fails to sign or initial a separate liquidated damage form for an increased deposit as required by paragraph 16. **Seller is not required to give Buyer a Notice to Perform regarding Close of Escrow.**
    (4) Notice To Buyer To Perform: The Notice to Buyer to Perform (C.A.R. Form NBP) shall: **(i)** be in writing; **(ii)** be signed by Seller; and **(iii)** give Buyer at least **24 (or ☐ _____) hours** (or until the time specified in the applicable paragraph, whichever occurs last) to take the applicable action. A Notice to Buyer to Perform may not be given any earlier than **2 Days** Prior to the expiration of the applicable time for Buyer to remove a contingency or cancel this Agreement or meet a 14C(3) obligation.

Buyer's Initials (_____)(_____)
Seller's Initials (_____)(_____)

Copyright © 1991-2007, CALIFORNIA ASSOCIATION OF REALTORS®, INC.

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

Print

D. **EFFECT OF BUYER'S REMOVAL OF CONTINGENCIES :** If Buyer removes, in writing, any contingency or cancellation rights, unless otherwise specified in a separate written agreement between Buyer and Seller, Buyer shall conclusively be deemed to have: **(i)** completed all Buyer Investigations, and review of reports and other applicable information and disclosures pertaining to that contingency or cancellation right; **(ii)** elected to proceed with the transaction; and **(iii)** assumed all liability, responsibility and expense for Repairs or corrections pertaining to that contingency or cancellation right, or for inability to obtain financing.

E. **EFFECT OF CANCELLATION ON DEPOSITS:** If Buyer or Seller gives written notice of cancellation pursuant to rights duly exercised under the terms of this Agreement, Buyer and Seller agree to Sign mutual instructions to cancel the sale and escrow and release deposits to the party entitled to the funds, less fees and costs incurred by that party. Fees and costs may be payable to service providers and vendors for services and products provided during escrow. **Release of funds will require mutual Signed release instructions from Buyer and Seller, judicial decision or arbitration award. A party may be subject to a civil penalty of up to $1,000 for refusal to sign such instructions if no good faith dispute exists as to who is entitled to the deposited funds (Civil Code §1057.3).**

15. **FINAL VERIFICATION OF CONDITION:** Buyer shall have the right to make a final inspection of the Property within **5 (or** _____**)** **Days** Prior to Close Of Escrow, NOT AS A CONTINGENCY OF THE SALE, but solely to confirm: **(i)** the Property is maintained pursuant to paragraph 7A; **(ii)** Repairs have been completed as agreed; and **(iii)** Seller has complied with Seller's other obligations under this Agreement.

16. **LIQUIDATED DAMAGES: If Buyer fails to complete this purchase because of Buyer's default, Seller shall retain, as liquidated damages, the deposit actually paid. If the Property is a dwelling with no more than four units, one of which Buyer intends to occupy, then the amount retained shall be no more than 3% of the purchase price. Any excess shall be returned to Buyer. Release of funds will require mutual, Signed release instructions from both Buyer and Seller, judicial decision or arbitration award.**
BUYER AND SELLER SHALL SIGN A SEPARATE LIQUIDATED DAMAGES PROVISION FOR ANY INCREASED DEPOSIT. (C.A.R. FORM RID)

Buyer's Initials _____/_____ **Seller's Initials** _____/_____

17. **DISPUTE RESOLUTION:**

A. **MEDIATION:** Buyer and Seller agree to mediate any dispute or claim arising between them out of this Agreement, or any resulting transaction, before resorting to arbitration or court action. Paragraphs 17B(2) and (3) below apply to mediation whether or not the Arbitration provision is initialed. Mediation fees, if any, shall be divided equally among the parties involved. If, for any dispute or claim to which this paragraph applies, any party commences an action without first attempting to resolve the matter through mediation, or refuses to mediate after a request has been made, then that party shall not be entitled to recover attorney fees, even if they would otherwise be available to that party in any such action. THIS MEDIATION PROVISION APPLIES WHETHER OR NOT THE ARBITRATION PROVISION IS INITIALED.

B. **ARBITRATION OF DISPUTES: (1) Buyer and Seller agree that any dispute or claim in Law or equity arising between them out of this Agreement or any resulting transaction, which is not settled through mediation, shall be decided by neutral, binding arbitration, including and subject to paragraphs 17B(2) and (3) below. The arbitrator shall be a retired judge or justice, or an attorney with at least 5 years of residential real estate Law experience, unless the parties mutually agree to a different arbitrator, who shall render an award in accordance with substantive California Law. The parties shall have the right to discovery in accordance with California Code of Civil Procedure §1283.05. In all other respects, the arbitration shall be conducted in accordance with Title 9 of Part III of the California Code of Civil Procedure. Judgment upon the award of the arbitrator(s) may be entered into any court having jurisdiction. Interpretation of this agreement to arbitrate shall be governed by the Federal Arbitration Act.**
(2) EXCLUSIONS FROM MEDIATION AND ARBITRATION: The following matters are excluded from mediation and arbitration: (i) a judicial or non-judicial foreclosure or other action or proceeding to enforce a deed of trust, mortgage or installment land sale contract as defined in California Civil Code §2985; (ii) an unlawful detainer action; (iii) the filing or enforcement of a mechanic's lien; and (iv) any matter that is within the jurisdiction of a probate, small claims or bankruptcy court. The filing of a court action to enable the recording of a notice of pending action, for order of attachment, receivership, injunction, or other provisional remedies, shall not constitute a waiver of the mediation and arbitration provisions.
(3) BROKERS: Buyer and Seller agree to mediate and arbitrate disputes or claims involving either or both Brokers, consistent with 17A and B, provided either or both Brokers shall have agreed to such mediation or arbitration prior to, or within a reasonable time after, the dispute or claim is presented to Brokers. Any election by either or both Brokers to participate in mediation or arbitration shall not result in Brokers being deemed parties to the Agreement.

"NOTICE: BY INITIALING IN THE SPACE BELOW YOU ARE AGREEING TO HAVE ANY DISPUTE ARISING OUT OF THE MATTERS INCLUDED IN THE 'ARBITRATION OF DISPUTES' PROVISION DECIDED BY NEUTRAL ARBITRATION AS PROVIDED BY CALIFORNIA LAW AND YOU ARE GIVING UP ANY RIGHTS YOU MIGHT POSSESS TO HAVE THE DISPUTE LITIGATED IN A COURT OR JURY TRIAL. BY INITIALING IN THE SPACE BELOW YOU ARE GIVING UP YOUR JUDICIAL RIGHTS TO DISCOVERY AND APPEAL, UNLESS THOSE RIGHTS ARE SPECIFICALLY INCLUDED IN THE 'ARBITRATION OF DISPUTES' PROVISION. IF YOU REFUSE TO SUBMIT TO ARBITRATION AFTER AGREEING TO THIS PROVISION, YOU MAY BE COMPELLED TO ARBITRATE UNDER THE AUTHORITY OF THE CALIFORNIA CODE OF CIVIL PROCEDURE. YOUR AGREEMENT TO THIS ARBITRATION PROVISION IS VOLUNTARY."

"WE HAVE READ AND UNDERSTAND THE FOREGOING AND AGREE TO SUBMIT DISPUTES ARISING OUT OF THE MATTERS INCLUDED IN THE 'ARBITRATION OF DISPUTES' PROVISION TO NEUTRAL ARBITRATION."

Buyer's Initials _____/_____ **Seller's Initials** _____/_____

Buyer's Initials (_____)(_____)
Seller's Initials (_____)(_____)

Reviewed by _____ Date _____

Copyright © 1991-2007, CALIFORNIA ASSOCIATION OF REALTORS®, INC.

Print

18. **PRORATIONS OF PROPERTY TAXES AND OTHER ITEMS:** Unless otherwise agreed in writing, the following items shall be PAID CURRENT and prorated between Buyer and Seller as of Close Of Escrow: real property taxes and assessments, interest, rents, HOA regular, special, and emergency dues and assessments imposed prior to Close Of Escrow, premiums on insurance assumed by Buyer, payments on bonds and assessments assumed by Buyer, and payments on Mello-Roos and other Special Assessment District bonds and assessments that are now a lien. The following items shall be assumed by Buyer WITHOUT CREDIT toward the purchase price: prorated payments on Mello-Roos and other Special Assessment District bonds and assessments and HOA special assessments that are now a lien but not yet due. Property will be reassessed upon change of ownership. Any supplemental tax bills shall be paid as follows: **(i)** for periods after Close Of Escrow, by Buyer; and **(ii)** for periods prior to Close Of Escrow, by Seller. TAX BILLS ISSUED AFTER CLOSE OF ESCROW SHALL BE HANDLED DIRECTLY BETWEEN BUYER AND SELLER. Prorations shall be made based on a 30-day month.
19. **WITHHOLDING TAXES:** Seller and Buyer agree to execute any instrument, affidavit, statement or instruction reasonably necessary to comply with federal (FIRPTA) and California withholding Law, if required (C.A.R. Forms AS and AB).
20. **MULTIPLE LISTING SERVICE ("MLS"):** Brokers are authorized to report to the MLS a pending sale and, upon Close Of Escrow, the terms of this transaction to be published and disseminated to persons and entities authorized to use the information on terms approved by the MLS.
21. **EQUAL HOUSING OPPORTUNITY:** The Property is sold in compliance with federal, state and local anti-discrimination Laws.
22. **ATTORNEY FEES:** In any action, proceeding, or arbitration between Buyer and Seller arising out of this Agreement, the prevailing Buyer or Seller shall be entitled to reasonable attorney fees and costs from the non-prevailing Buyer or Seller, except as provided in paragraph 17A.
23. **SELECTION OF SERVICE PROVIDERS:** If Brokers refer Buyer or Seller to persons, vendors, or service or product providers ("Providers"), Brokers do not guarantee the performance of any Providers. Buyer and Seller may select ANY Providers of their own choosing.
24. **TIME OF ESSENCE; ENTIRE CONTRACT; CHANGES:** Time is of the essence. All understandings between the parties are incorporated in this Agreement. Its terms are intended by the parties as a final, complete and exclusive expression of their Agreement with respect to its subject matter, and may not be contradicted by evidence of any prior agreement or contemporaneous oral agreement. If any provision of this Agreement is held to be ineffective or invalid, the remaining provisions will nevertheless be given full force and effect. **Neither this Agreement nor any provision in it may be extended, amended, modified, altered or changed, except in writing Signed by Buyer and Seller.**
25. **OTHER TERMS AND CONDITIONS,** including attached supplements:
    A. ☑ Buyer's Inspection Advisory (C.A.R. Form BIA)
    B. ☐ Purchase Agreement Addendum (C.A.R. Form PAA paragraph numbers:)
    C. ☐ Statewide Buyer and Seller Advisory (C.A.R. Form SBSA)
    D. ☐ Seller shall provide Buyer with a completed Seller Property Questionnaire (C.A.R. form SPQ) within the time specified in paragraph 14A
    E. _____
26. **DEFINITIONS:** As used in this Agreement:
    A. **"Acceptance"** means the time the offer or final counter offer is accepted in writing by a party and is delivered to and personally received by the other party or that party's authorized agent in accordance with the terms of this offer or a final counter offer.
    B. **"Agreement"** means the terms and conditions of this accepted California Residential Purchase Agreement and any accepted counter offers and addenda.
    C. **"C.A.R. Form"** means the specific form referenced or another comparable form agreed to by the parties.
    D. **"Close Of Escrow"** means the date the grant deed, or other evidence of transfer of title, is recorded. If the scheduled close of escrow falls on a Saturday, Sunday or legal holiday, then close of escrow shall be the next business day after the scheduled close of escrow date.
    E. **"Copy"** means copy by any means including photocopy, NCR, facsimile and electronic.
    F. **"Days"** means calendar days, unless otherwise required by Law.
    G. **"Days After"** means the specified number of calendar days after the occurrence of the event specified, not counting the calendar date on which the specified event occurs, and ending at 11:59PM on the final day.
    H. **"Days Prior"** means the specified number of calendar days before the occurrence of the event specified, not counting the calendar date on which the specified event is scheduled to occur.
    I. **"Electronic Copy" or "Electronic Signature"** means, as applicable, an electronic copy or signature complying with California Law. Buyer and Seller agree that electronic means will not be used by either party to modify or alter the content or integrity of this Agreement without the knowledge and consent of the other.
    J. **"Law"** means any law, code, statute, ordinance, regulation, rule or order, which is adopted by a controlling city, county, state or federal legislative, judicial or executive body or agency.
    K. **"Notice to Buyer to Perform"** means a document (C.A.R. Form NBP), which shall be in writing and Signed by Seller and shall give Buyer at least 24 hours **(or as otherwise specified in paragraph 14C(4))** to remove a contingency or perform as applicable.
    L. **"Repairs"** means any repairs (including pest control), alterations, replacements, modifications or retrofitting of the Property provided for under this Agreement.
    M. **"Signed"** means either a handwritten or electronic signature on an original document, Copy or any counterpart.
    N. **Singular and Plural** terms each include the other, when appropriate.

Copyright © 1991-2007, CALIFORNIA ASSOCIATION OF REALTORS®, INC.

27. AGENCY:

A. DISCLOSURE: Buyer and Seller each acknowledge prior receipt of C.A.R. Form AD "Disclosure Regarding Real Estate Agency Relationships."

B. POTENTIALLY COMPETING BUYERS AND SELLERS: Buyer and Seller each acknowledge receipt of a disclosure of the possibility of multiple representation by the Broker representing that principal. This disclosure may be part of a listing agreement, buyer-broker agreement or separate document (C.A.R. Form DA). Buyer understands that Broker representing Buyer may also represent other potential buyers, who may consider, make offers on or ultimately acquire the Property. Seller understands that Broker representing Seller may also represent other sellers with competing properties of interest to this Buyer.

C. CONFIRMATION: The following agency relationships are hereby confirmed for this transaction:
Listing Agent _____ (Print Firm Name) is the agent of (check one): ☐ the Seller exclusively; or ☐ both the Buyer and Seller.
Selling Agent _____ (Print Firm Name) (if not same as Listing Agent) is the agent of (check one): ☐ the Buyer exclusively; or ☐ the Seller exclusively; or ☐ both the Buyer and Seller. Real Estate Brokers are not parties to the Agreement between Buyer and Seller.

28. JOINT ESCROW INSTRUCTIONS TO ESCROW HOLDER:

A. The following paragraphs, or applicable portions thereof, of this Agreement constitute the joint escrow instructions of Buyer and Seller to Escrow Holder, which Escrow Holder is to use along with any related counter offers and addenda, and any additional mutual instructions to close the escrow: 1, 2, 4, 12, 13B, 14E, 18, 19, 24, 25B and 25D, 26, 28, 29, 32A, 33 and paragraph D of the section titled Real Estate Brokers on page 8. If a Copy of the separate compensation agreement(s) provided for in paragraph 29 or 32A, or paragraph D of the section titled Real Estate Brokers on page 8 is deposited with Escrow Holder by Broker, Escrow Holder shall accept such agreement(s) and pay out from Buyer's or Seller's funds, or both, as applicable, the Broker's compensation provided for in such agreement(s). The terms and conditions of this Agreement not set forth in the specified paragraphs are additional matters for the information of Escrow Holder, but about which Escrow Holder need not be concerned. Buyer and Seller will receive Escrow Holder's general provisions directly from Escrow Holder and will execute such provisions upon Escrow Holder's request. To the extent the general provisions are inconsistent or conflict with this Agreement, the general provisions will control as to the duties and obligations of Escrow Holder only. Buyer and Seller will execute additional instructions, documents and forms provided by Escrow Holder that are reasonably necessary to close the escrow.

B. A Copy of this Agreement shall be delivered to Escrow Holder within **3** business days after Acceptance (or ☐ _____). Buyer and Seller authorize Escrow Holder to accept and rely on Copies and Signatures as defined in this Agreement as originals, to open escrow and for other purposes of escrow. The validity of this Agreement as between Buyer and Seller is not affected by whether or when Escrow Holder Signs this Agreement.

C. Brokers are a party to the escrow for the sole purpose of compensation pursuant to paragraphs 29, 32A and paragraph D of the section titled Real Estate Brokers on page 8. Buyer and Seller irrevocably assign to Brokers compensation specified in paragraphs 29 and 32A, respectively, and irrevocably instruct Escrow Holder to disburse those funds to Brokers at Close Of Escrow or pursuant to any other mutually executed cancellation agreement. Compensation instructions can be amended or revoked only with the written consent of Brokers. Escrow Holder shall immediately notify Brokers: **(i)** if Buyer's initial or any additional deposit is not made pursuant to this Agreement, or is not good at time of deposit with Escrow Holder; or **(ii)** if Buyer and Seller instruct Escrow Holder to cancel escrow.

D. A Copy of any amendment that affects any paragraph of this Agreement for which Escrow Holder is responsible shall be delivered to Escrow Holder within **2** business days after mutual execution of the amendment.

29. BROKER COMPENSATION FROM BUYER: If applicable, upon Close Of Escrow, **Buyer** agrees to pay compensation to Broker as specified in a separate written agreement between Buyer and Broker.

30. TERMS AND CONDITIONS OF OFFER:

This is an offer to purchase the Property on the above terms and conditions. All paragraphs with spaces for initials by Buyer and Seller are incorporated in this Agreement only if initialed by all parties. If at least one but not all parties initial, a counter offer is required until agreement is reached. Seller has the right to continue to offer the Property for sale and to accept any other offer at any time prior to notification of Acceptance. Buyer has read and acknowledges receipt of a Copy of the offer and agrees to the above confirmation of agency relationships. If this offer is accepted and Buyer subsequently defaults, Buyer may be responsible for payment of Brokers' compensation. This Agreement and any supplement, addendum or modification, including any Copy, may be Signed in two or more counterparts, all of which shall constitute one and the same writing.

Buyer's Initials (_____)(_____)
Seller's Initials (_____)(_____)
Reviewed by _____ Date _____

Copyright © 1991-2007, CALIFORNIA ASSOCIATION OF REALTORS®, INC.

Print

Property Address: _____ Date: _____

31. **EXPIRATION OF OFFER:** This offer shall be deemed revoked and the deposit shall be returned unless the offer is Signed by Seller and a Copy of the Signed offer is personally received by Buyer, or by _____, who is authorized to receive it by 5:00 PM on the third Day after this offer is signed by Buyer (or, if checked, ☐ by _____ (date), at _____ AM/PM).

Date _____ Date _____

BUYER _____ BUYER _____

(Print name) **(Print name)**

(Address)

32. **BROKER COMPENSATION FROM SELLER:**
    A. Upon Close Of Escrow, Seller agrees to pay compensation to Broker as specified in a separate written agreement between Seller and Broker.
    B. If escrow does not close, compensation is payable as specified in that separate written agreement.
33. **ACCEPTANCE OF OFFER:** Seller warrants that Seller is the owner of the Property, or has the authority to execute this Agreement. Seller accepts the above offer, agrees to sell the Property on the above terms and conditions, and agrees to the above confirmation of agency relationships. Seller has read and acknowledges receipt of a Copy of this Agreement, and authorizes Broker to deliver a Signed Copy to Buyer.
    ☐ (If checked) **SUBJECT TO ATTACHED COUNTER OFFER, DATED** _____.

Date _____ Date _____

SELLER _____ SELLER _____

(Print name) **(Print name)**

(Address)

(____/____) (Initials) **CONFIRMATION OF ACCEPTANCE:** A Copy of Signed Acceptance was personally received by Buyer or Buyer's authorized agent on (date) _____ at _____ AM/PM. **A binding Agreement is created when a Copy of Signed Acceptance is personally received by Buyer or Buyer's authorized agent whether or not confirmed in this document. Completion of this confirmation is not legally required in order to create a binding Agreement; it is solely intended to evidence the date that Confirmation of Acceptance has occurred.**

REAL ESTATE BROKERS:

A. Real Estate Brokers are not parties to the Agreement between Buyer and Seller.
B. Agency relationships are confirmed as stated in paragraph 27.
C. If specified in paragraph 2A, Agent who submitted the offer for Buyer acknowledges receipt of deposit.
D. **COOPERATING BROKER COMPENSATION:** Listing Broker agrees to pay Cooperating Broker **(Selling Firm)** and Cooperating Broker agrees to accept, out of Listing Broker's proceeds in escrow: **(i)** the amount specified in the MLS, provided Cooperating Broker is a Participant of the MLS in which the Property is offered for sale or a reciprocal MLS; or **(ii)** ☐ (if checked) the amount specified in a separate written agreement (C.A.R. Form CBC) between Listing Broker and Cooperating Broker.

Real Estate Broker (Selling Firm) _____ DRE Lic. # _____
By _____ DRE Lic. # _____ Date _____
Address _____ City _____ State _____ Zip _____
Telephone _____ Fax _____ E-mail _____

Real Estate Broker (Listing Firm) _____ DRE Lic. # _____
By _____ DRE Lic. # _____ Date _____
Address _____ City _____ State _____ Zip _____
Telephone _____ Fax _____ E-mail _____

ESCROW HOLDER ACKNOWLEDGMENT:

Escrow Holder acknowledges receipt of a Copy of this Agreement, (if checked, ☐ a deposit in the amount of $ _____), counter offer numbers _____ and _____, and agrees to act as Escrow Holder subject to paragraph 28 of this Agreement, any supplemental escrow instructions and the terms of Escrow Holder's general provisions.

Escrow Holder is advised that the date of Confirmation of Acceptance of the Agreement as between Buyer and Seller is _____

Escrow Holder _____ Escrow # _____
By _____ Date _____
Address _____
Phone/Fax/E-mail _____
Escrow Holder is licensed by the California Department of ☐ Corporations, ☐ Insurance, ☐ Real Estate. License # _____

(____/____) (Seller's Initials) **REJECTION OF OFFER:** No counter offer is being made. This offer was reviewed and rejected by Seller on _____ (Date)

THIS FORM HAS BEEN APPROVED BY THE CALIFORNIA ASSOCIATION OF REALTORS® (C.A.R.). NO REPRESENTATION IS MADE AS TO THE LEGAL VALIDITY OR ADEQUACY OF ANY PROVISION IN ANY SPECIFIC TRANSACTION. A REAL ESTATE BROKER IS THE PERSON QUALIFIED TO ADVISE ON REAL ESTATE TRANSACTIONS. IF YOU DESIRE LEGAL OR TAX ADVICE, CONSULT AN APPROPRIATE PROFESSIONAL.
This form is available for use by the entire real estate industry. It is not intended to identify the user as a REALTOR®. REALTOR® is a registered collective membership mark which may be used only by members of the NATIONAL ASSOCIATION OF REALTORS® who subscribe to its Code of Ethics.

Published and Distributed by:
REAL ESTATE BUSINESS SERVICES, INC.
a subsidiary of the California Association of REALTORS®
525 South Virgil Avenue, Los Angeles, California 90020

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/6 Residential Purchase and Sale Transactions/ §6.25 2. Form: Buyer's Inspection Advisory (CAR Form BIA)

§6.25 2. Form: Buyer's Inspection Advisory (CAR Form BIA)

Print

CALIFORNIA ASSOCIATION OF REALTORS®

BUYER'S INSPECTION ADVISORY

(C.A.R. Form BIA, Revised 10/02)

Property Address: _____ ("Property").

A. IMPORTANCE OF PROPERTY INVESTIGATION: The physical condition of the land and improvements being purchased is not guaranteed by either Seller or Brokers. For this reason, you should conduct thorough investigations of the Property personally and with professionals who should provide written reports of their investigations. A general physical inspection typically does not cover all aspects of the Property nor items affecting the Property that are not physically located on the Property. If the professionals recommend further investigations, including a recommendation by a pest control operator to inspect inaccessible areas of the Property, you should contact qualified experts to conduct such additional investigations.

B. BUYER RIGHTS AND DUTIES: You have an affirmative duty to exercise reasonable care to protect yourself, including discovery of the legal, practical and technical implications of disclosed facts, and the investigation and verification of information and facts that you know or that are within your diligent attention and observation. The purchase agreement gives you the right to investigate the Property. If you exercise this right, and you should, you must do so in accordance with the terms of that agreement. This is the best way for you to protect yourself. It is extremely important for you to read all written reports provided by professionals and to discuss the results of inspections with the professional who conducted the inspection. You have the right to request that Seller make repairs, corrections or take other action based upon items discovered in your investigations or disclosed by Seller. If Seller is unwilling or unable to satisfy your requests, or you do not want to purchase the Property in its disclosed and discovered condition, you have the right to cancel the agreement if you act within specific time periods. If you do not cancel the agreement in a timely and proper manner, you may be in breach of contract.

C. SELLER RIGHTS AND DUTIES: Seller is required to disclose to you material facts known to him/her that affect the value or desirability of the Property. However, Seller may not be aware of some Property defects or conditions. Seller does not have an obligation to inspect the Property for your benefit nor is Seller obligated to repair, correct or otherwise cure known defects that are disclosed to you or previously unknown defects that are discovered by you or your inspectors during escrow. The purchase agreement obligates Seller to make the Property available to you for investigations.

D. BROKER OBLIGATIONS: Brokers do not have expertise in all areas and therefore cannot advise you on many items, such as soil stability, geologic or environmental conditions, hazardous or illegal controlled substances, structural conditions of the foundation or other improvements, or the condition of the roof, plumbing, heating, air conditioning, electrical, sewer, septic, waste disposal, or other system. The only way to accurately determine the condition of the Property is through an inspection by an appropriate professional selected by you. If Broker gives you referrals to such professionals, Broker does not guarantee their performance. You may select any professional of your choosing. In sales involving residential dwellings with no more than four units, Brokers have a duty to make a diligent visual inspection of the accessible areas of the Property and to disclose the results of that inspection. However, as some Property defects or conditions may not be discoverable from a visual inspection, it is possible Brokers are not aware of them. If you have entered into a written agreement with a Broker, the specific terms of that agreement will determine the nature and extent of that Broker's duty to you. **YOU ARE STRONGLY ADVISED TO INVESTIGATE THE CONDITION AND SUITABILITY OF ALL ASPECTS OF THE PROPERTY. IF YOU DO NOT DO SO, YOU ARE ACTING AGAINST THE ADVICE OF BROKERS.**

E. YOU ARE ADVISED TO CONDUCT INVESTIGATIONS OF THE ENTIRE PROPERTY, INCLUDING, BUT NOT LIMITED TO THE FOLLOWING:

1. **GENERAL CONDITION OF THE PROPERTY, ITS SYSTEMS AND COMPONENTS:** Foundation, roof, plumbing, heating, air conditioning, electrical, mechanical, security, pool/spa, other structural and non-structural systems and components, fixtures, built-in appliances, any personal property included in the sale, and energy efficiency of the Property. (Structural engineers are best suited to determine possible design or construction defects, and whether improvements are structurally sound.)
2. **SQUARE FOOTAGE, AGE, BOUNDARIES:** Square footage, room dimensions, lot size, age of improvements and boundaries. Any numerical statements regarding these items are APPROXIMATIONS ONLY and have not been verified by Seller and cannot be verified by Brokers. Fences, hedges, walls, retaining walls and other natural or constructed barriers or markers do not necessarily identify true Property boundaries. (Professionals such as appraisers, architects, surveyors and civil engineers are best suited to determine square footage, dimensions and boundaries of the Property.)
3. **WOOD DESTROYING PESTS:** Presence of, or conditions likely to lead to the presence of wood destroying pests and organisms and other infestation or infection. Inspection reports covering these items can be separated into two sections: Section 1 identifies areas where infestation or infection is evident. Section 2 identifies areas where there are conditions likely to lead to infestation or infection. A registered structural pest control company is best suited to perform these inspections.

The copyright laws of the United States (Title 17 U.S. Code) forbid the unauthorized reproduction of this form, or any portion thereof, by photocopy machine or any other means, including facsimile or computerized formats. Copyright © 1991-2002, CALIFORNIA ASSOCIATION OF REALTORS®, INC. ALL RIGHTS RESERVED.

Buyer's Initials (_____)(_____)
Seller's Initials (_____)(_____)

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

Print

Property Address: _____ Date: _____

4. **SOIL STABILITY:** Existence of fill or compacted soil, expansive or contracting soil, susceptibility to slippage, settling or movement, and the adequacy of drainage. (Geotechnical engineers are best suited to determine such conditions, causes and remedies.)
5. **ROOF:** Present condition, age, leaks, and remaining useful life. (Roofing contractors are best suited to determine these conditions.)
6. **POOL/SPA:** Cracks, leaks or operational problems. (Pool contractors are best suited to determine these conditions.)
7. **WASTE DISPOSAL:** Type, size, adequacy, capacity and condition of sewer and septic systems and components, connection to sewer, and applicable fees.
8. **WATER AND UTILITIES; WELL SYSTEMS AND COMPONENTS:** Water and utility availability, use restrictions and costs. Water quality, adequacy, condition, and performance of well systems and components.
9. **ENVIRONMENTAL HAZARDS:** Potential environmental hazards, including, but not limited to, asbestos, lead-based paint and other lead contamination, radon, methane, other gases, fuel oil or chemical storage tanks, contaminated soil or water, hazardous waste, waste disposal sites, electromagnetic fields, nuclear sources, and other substances, materials, products, or conditions (including mold (airborne, toxic or otherwise), fungus or similar contaminants). (For more in formation on these items, you may consult an appropriate professional or read the booklets "Environmental Hazards: A Guide for Homeowners ,Buyers, Landlords and Tenants," "Protect Your Family From Lead in Your Home" or both.)
10. **EARTHQUAKES AND FLOODING:** Susceptibility of the Property to earthquake/seismic hazards and propensity of the Property to flood. (A Geologist or Geotechnical Engineer is best suited to provide information on these conditions.)
11. **FIRE, HAZARD AND OTHER INSURANCE:** The availability and cost of necessary or desired insurance may vary. The location of the Property in a seismic, flood or fire hazard zone, and other conditions, such as the age of the Property and the claims history of the Property and Buyer, may affect the availability and need for certain types of insurance. Buyer should explore insurance options early as this information may affect other decisions, including the removal of loan and inspection contingencies. (An insurance agent is best suited to provide information on these conditions.)
12. **BUILDING PERMITS, ZONING AND GOVERNMENTAL REQUIREMENTS:** Permits, inspections, certificates, zoning, other governmental limitations, restrictions, and requirements affecting the current or future use of the Property, its development or size. (Such information is available from appropriate governmental agencies and private information providers. Brokers are not qualified to review or interpret any such information.)
13. **RENTAL PROPERTY RESTRICTIONS:** Some cities and counties impose restrictions that limit the amount of rent that can be charged, the maximum number of occupants, and the right of a landlord to terminate a tenancy. Deadbolt or other locks and security systems for doors and windows, including window bars, should be examined to determine whether they satisfy legal requirements. (Government agencies can provide information about these restrictions and other requirements.)
14. **SECURITY AND SAFETY:** State and local Law may require the installation of barriers, access alarms, self-latching mechanisms and/or other measures to decrease the risk to children and other persons of existing swimming pools and hot tubs, as well as various fire safety and other measures concerning other features of the Property. Compliance requirements differ from city to city and county to county. Unless specifically agreed, the Property may not be in compliance with these requirements. (Local government agencies can provide information about these restrictions and other requirements.)
15. **NEIGHBORHOOD, AREA, SUBDIVISION CONDITIONS; PERSONAL FACTORS:** Neighborhood or area conditions, including schools, proximity and adequacy of law enforcement, crime statistics, the proximity of registered felons or offenders, fire protection, other government services, availability, adequacy and cost of any speed-wired, wireless internet connections or other telecommunications or other technology services and installations, proximity to commercial, industrial or agricultural activities, existing and proposed transportation, construction and development that may affect noise, view, or traffic, airport noise, noise or odor from any source, wild and domestic animals, other nuisances, hazards, or circumstances, protected species, wetland properties, botanical diseases, historic or other governmentally protected sites or improvements, cemeteries, facilities and condition of common areas of common interest subdivisions, and possible lack of compliance with any governing documents or Homeowners' Association requirements, conditions and influences of significance to certain cultures and/or religions, and personal needs, requirements and preferences of Buyer.

Buyer and Seller acknowledge and agree that Broker: **(i)** Does not decide what price Buyer should pay or Seller should accept; **(ii)** Does not guarantee the condition of the Property; **(iii)** Does not guarantee the performance, adequacy or completeness of inspections, services, products or repairs provided or made by Seller or others; **(iv)** Shall not be responsible for identifying defects that are not known to Broker and **(a)** are not visually observable in reasonably accessible areas of the Property; **(b)** are in common areas; or **(c)** are off the site of the Property; **(v)** Shall not be responsible for inspecting public records or permits concerning the title or use of Property; **(vi)** Shall not be responsible for identifying the location of boundary lines or other items affecting title; **(vii)** Shall not be responsible for verifying square footage, representations of others or information contained in Investigation reports, Multiple Listing Service, advertisements, flyers or other promotional material; **(viii)** Shall not be responsible for providing legal or tax advice regarding any aspect of a transaction entered into by Buyer or Seller; and **(ix)** Shall not be responsible for providing other advice or information that exceeds the knowledge, education and experience required to perform real estate licensed activity. Buyer and Seller agree to seek legal, tax, insurance, title and other desired assistance from appropriate professionals.

By signing below, Buyer and Seller each acknowledge that they have read, understand, accept and have received a Copy of this Advisory. Buyer is encouraged to read it carefully.

Buyer Signature	Date	Buyer Signature	Date
Seller Signature	Date	Seller Signature	Date

THIS FORM HAS BEEN APPROVED BY THE CALIFORNIA ASSOCIATION OF REALTORS® (C.A.R.). NO REPRESENTATION IS MADE AS TO THE LEGAL VALIDITY OR ADEQUACY OF ANY PROVISION IN ANY SPECIFIC TRANSACTION. A REAL ESTATE BROKER IS THE PERSON QUALIFIED TO ADVISE ON REAL ESTATE TRANSACTIONS. IF YOU DESIRE LEGAL OR TAX ADVICE, CONSULT AN APPROPRIATE PROFESSIONAL.

This form is available for use by the entire real estate industry. It is not intended to identify the user as a REALTOR®. REALTOR® is a registered collective membership mark which may be used only by members of the NATIONAL ASSOCIATION OF REALTORS® who subscribe to its Code of Ethics.

SURE TRAC The System for Success™

Published by the California Association of REALTORS®

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

BUYER'S INSPECTION ADVISORY (BIA PAGE 2 OF 2)

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/6 Residential Purchase and Sale Transactions/ §6.26 3. Form: Purchase Agreement Addendum (CAR Form PAA)

§6.26 3. Form: Purchase Agreement Addendum (CAR Form PAA)

Print

CALIFORNIA ASSOCIATION OF REALTORS®

PURCHASE AGREEMENT ADDENDUM No. _____

(May Also Be Used With Counter Offer)

(C.A.R. Form PAA, Revised 4/08)

This is an addendum to the ☐ California Residential Purchase Agreement, ☐ Counter Offer No. _____, ☐ Other _____ _____, ("Agreement"), dated _____, on property known as _____ x, _____ ("Property"), between _____ ("Buyer"), and _____ ("Seller").
(The definitions in the California Residential Purchase Agreement are applicable to this Purchase Agreement Addendum.)

1. ☐ **CANCELLATION OF PRIOR SALE; BACK-UP OFFER** (If checked): This Agreement is in back-up position number _____, and is contingent upon written cancellation of any prior contracts and related escrows ("Prior Contracts") between Seller and other buyers. Seller and other buyers may mutually agree to modify or amend the terms of Prior Contracts. Buyer may cancel this Agreement in writing at any time before Seller provides Buyer Copies of written cancellations of Prior Contracts Signed by all parties to those contracts. If Seller is unable to provide such written Signed cancellations to Buyer by _____ (date), then either Buyer or Seller may cancel the Agreement in writing.
   A. **BUYER'S DEPOSIT CHECK** shall be: **(i)** held uncashed until Copies of the written cancellations Signed by all parties to the Prior Contracts are provided to Buyer; OR **(ii)** (if checked) ☐ immediately handled as provided in the Agreement.
   B. **TIME PERIODS** in the Agreement for Investigations, contingencies, covenants and other obligations **(i)** shall begin on the Day After Seller provides Buyer Copies of Signed cancellations of Prior Contracts; OR **(ii)** (if checked) ☐ all time periods shall begin as provided in this Agreement. However, if the date for Close Of Escrow is a specific calendar date, that date shall NOT be extended, unless agreed to in writing by Buyer and Seller.
2. ☐ **SELLER TO REMAIN IN POSSESSION AFTER CLOSE OF ESCROW** (If checked): This provision is intended for short-term occupancy (i.e. less than 30 Days). If occupancy is intended to be for 30 Days or longer, use Residential Lease After Sale (C.A.R. Form RLAS). **Note: Local rent control or other Law regarding tenant's rights may impact Buyer's and Seller's rights and obligations.**
   A. **TERM:** Seller to remain in possession of Property for _____ **Days** After Close Of Escrow (or ☐ _____). Seller has no right to remain in possession beyond this term and may be responsible for court awarded damages if Seller does remain.
   B. **COMPENSATION:** Seller agrees to pay Buyer (i) for the term specified in 2A, $ _____ per Day (or ☐ _____), and (ii) a security deposit in the amount of $ _____. Seller shall deposit such funds with escrow holder prior to Close Of Escrow or such funds shall be withheld from Seller's proceeds. At Close Of Escrow, security deposit will be released to Buyer (or ☐ held in escrow).
   C. **LATE CHARGE/NSF CHECKS:** If any payment from Seller to Buyer is required outside of escrow, and any such payment is not received by Buyer within **5 (or** ☐ _____ **) Days** After date due, Seller shall pay to Buyer an additional sum of $ _____ as a Late Charge. If a check is returned for non-sufficient funds ("NSF"), Seller shall pay to Buyer $25.00 as an NSF charge. Seller and Buyer agree that these charges represent a fair and reasonable estimate of the costs Buyer may incur by reason of Seller's late or NSF payment. Buyer's acceptance of any Late Charge or NSF fee shall not constitute a waiver as to any default by Seller.
   D. **UTILITIES:** Seller agrees to pay for all utilities and services, and the following charges: _____ _____ except _____, which shall be paid for by Buyer.
   E. **ENTRY:** Seller shall make Property available to Buyer for the purpose of entering to make necessary or agreed repairs, or to supply necessary or agreed services, or to show Property to prospective or actual purchasers, tenants, mortgagees, lenders, appraisers or contractors. Buyer and Seller agree that 24 hours notice (oral or written) shall be reasonable and sufficient notice. In an emergency, Buyer may enter Property at any time without prior notice.
   F. **MAINTENANCE:** Seller shall maintain the Property, including pool, spa, landscaping and grounds, and all personal property included in the sale in substantially the same condition as on the date of Acceptance of the Agreement. Except as provided in the Agreement, Seller shall not make alterations to the Property without Buyer's written consent.
   G. **ASSIGNMENT; SUBLETTING:** Seller shall not assign or sublet all or any part of the Property, or assign or transfer the right to occupy the Property. Any assignment, subletting or transfer of the Property by voluntary act of Seller, by operation of Law or otherwise, without Buyer's prior written consent shall give Buyer the right to terminate Seller's right to possession.
   H. **SELLER'S OBLIGATIONS UPON DELIVERY OF POSSESSION:** Upon delivery of possession to Buyer, Seller shall deliver the Property in the condition and on the terms provided in the Agreement.
   I. **INSURANCE:** Seller's personal property (including vehicles) is not insured by Buyer, and, if applicable, owner's association, against loss or damage due to fire, theft, vandalism, rain, water, criminal or negligent acts of others, or any other cause. Seller is to carry Seller's own insurance to protect Seller from such loss.
   J. **WAIVER:** The waiver of any breach shall not be construed as a continuing waiver of the same or any subsequent breach.
   K. **OTHER TERMS AND CONDITIONS/SUPPLEMENTS:** _____ _____ _____

The copyright laws of the United States (Title 17 U.S. Code) forbid the unauthorized reproduction of this form, or any portion thereof, by photocopy machine or any other means, including facsimile or computerized formats. Copyright © 1991-2008, CALIFORNIA ASSOCIATION OF REALTORS®, INC. ALL RIGHTS RESERVED.

Buyer's Initials (_____) (_____)
Seller's Initials (_____) (_____)
Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

Agent: Howard Pearlman Phone: (925)9358555 Fax: 925-935-1819 Prepared using WINForms® software
Broker: Howard Pearlman 646 Brookrose Dr Walnut Creek CA 94596

3. ☐ **TENANT TO REMAIN IN POSSESSION** (If checked): Buyer shall take Property subject to the rights of existing tenants. Seller shall, within **7 (or** ☐ _____ **) Days** After Acceptance, deliver to Buyer Copies of all: estoppel certificates sent to and received back from tenants; leases; rental agreements; and current income and expense statements ("Rental Documents"). Seller shall give Buyer written notice of any changes to existing leases or tenancies or new agreements to lease or rent ("Proposed Changes") at least **7 (or** ☐ _____ **) Days** prior to any Proposed Changes. Buyer's approval of the Rental Documents and Proposed Changes is a contingency of the Agreement. Buyer shall, within **5 (or** ☐ _____ **) Days** After receipt of Rental Documents or Proposed Changes remove the applicable contingency or cancel the Agreement. Seller shall transfer to Buyer, through escrow, all unused tenant deposits. No warranty is made concerning compliance with governmental restrictions, if any, limiting the amount of rent that can lawfully be charged, and/or the maximum number of persons who can lawfully occupy the Property, unless otherwise agreed in writing.
4. ☐ **SECONDARY OR ASSUMED LOAN** (If checked): Obtaining the secondary loan or assumption below and approval of such financing is a contingency of this Agreement. Buyer shall act diligently and in good faith to obtain the designated financing.
   A. ☐ **SECONDARY LOAN:**
   (1) New second deed of trust in favor of LENDER encumbering the Property, securing a note payable at maximum interest of _____ % fixed rate or _____ % initial adjustable rate, with a maximum interest rate of _____ %, balance due in _____ years. Buyer shall pay loan fees/points not to exceed _____. (These terms apply whether the designated loan is conventional, FHA or VA.)
   (2) Within **17 (or** ☐ _____ **Days)** After Acceptance, Buyer shall, as specified in the Agreement, remove this contingency or cancel this Agreement; OR (if checked) ☐ secondary loan contingency shall remain in effect until the loan is funded.
   B. ☐ **ASSUMPTION OF EXISTING LOAN:**
   (1) Assumption of existing deed of trust encumbering the Property, securing a note payable at maximum interest of _____ % fixed rate or _____ % initial adjustable rate, with a maximum interest rate of _____ %, balance due in _____ years. Buyer shall pay loan fees/points not to exceed _____. Seller shall, within **5 (or** ☐ _____ **) Days** After Acceptance, request from Lender, and upon receipt provide to Buyer, Copies of all applicable notes and deeds of trust, loan balances and current interest rates. Differences between estimated and actual loan balances shall be adjusted at Close Of Escrow by cash down payment. Impound accounts, if any, shall be assigned and charged to Buyer and credited to Seller. If this is an assumption of a VA Loan, the sale is contingent upon Seller being provided a release of liability and substitution of eligibility, unless otherwise agreed in writing.
   (2) Within **17 (or** ☐ _____ **) Days** After Acceptance, Buyer shall, as specified in the Agreement, remove this contingency or cancel this Agreement. However, if the assumed loan documents are not provided to Buyer within **7 Days After Acceptance,** Buyer has **5 (or** ☐ _____ **) Days** After receipt of these documents, or the fixed time specified in 4B(2), whichever occurs last, to remove this contingency or cancel the Agreement; OR (if checked) ☐ assumed loan contingency shall remain in effect until the assumption is approved.
5. ☐ **COURT CONFIRMATION** (If checked): This Agreement is contingent upon court confirmation on or before _____ (date). If court confirmation is not obtained by that date, Buyer may cancel this Agreement in writing. Court confirmation may be required in probate, conservatorship, guardianship, receivership, bankruptcy or other proceedings. The court may allow open, competitive bidding, resulting in Property being sold to the highest bidder. Broker recommends that Buyer appear at the court confirmation hearing. Buyer understands that **(i)** Broker and others may continue to market the Property and **(ii)** Broker may represent other competitive bidders prior to and at the court confirmation.

By signing below Buyer and Seller acknowledge that each has read, understands, received a copy of and agrees to the terms of this Purchase Agreement Addendum.

Date _____ Date _____

Buyer _____ Seller _____

Buyer _____ Seller _____

THIS FORM HAS BEEN APPROVED BY THE CALIFORNIA ASSOCIATION OF REALTORS® (C.A.R.). NO REPRESENTATION IS MADE AS TO THE LEGAL VALIDITY OR ADEQUACY OF ANY PROVISION IN ANY SPECIFIC TRANSACTION. A REAL ESTATE BROKER IS THE PERSON QUALIFIED TO ADVISE ON REAL ESTATE TRANSACTIONS. IF YOU DESIRE LEGAL OR TAX ADVICE, CONSULT AN APPROPRIATE PROFESSIONAL.
This form is available for use by the entire real estate industry. It is not intended to identify the user as a REALTOR®. REALTOR® is a registered collective membership mark which may be used only by members of the NATIONAL ASSOCIATION OF REALTORS® who subscribe to its Code of Ethics.

Published and Distributed by:
REAL ESTATE BUSINESS SERVICES, INC.
a subsidiary of the California Association of REALTORS®
525 South Virgil Avenue, Los Angeles, California 90020

EQUAL HOUSING OPPORTUNITY

Reviewed by _____ Date _____

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/6 Residential Purchase and Sale Transactions/ §6.27 4. Form: Statewide Buyer and Seller Advisory (CAR Form SBSA)

§6.27 4. Form: Statewide Buyer and Seller Advisory (CAR Form SBSA)

Print

CALIFORNIA ASSOCIATION OF REALTORS®

STATEWIDE BUYER AND SELLER ADVISORY
(This Form Does Not Replace Local Condition Disclosures.
Additional Addenda May Be Attached to This Advisory. See Paragraph 44)
(C.A.R. Form SBSA, Revised 4/07)

Property Address: _____ ("Property").

BUYER RIGHTS AND DUTIES:
- The physical condition of the land and improvements being purchased are not guaranteed by Seller or Brokers.
- You should conduct thorough investigations of the Property personally and with appropriate professionals.
- If professionals recommend further inspections, you should contact qualified experts to conduct such inspections.
- You should retain your own professional even if Seller or Broker has provided you with existing reports.
- You should read all written reports given to you and discuss those reports with the persons who prepared them.
- Your have the right to request that the Seller make repairs, corrections or take other actions based on inspections or disclosures.
- If the Seller is unwilling or unable to satisfy your requests, and you act within certain time periods, you may have the right to cancel the agreement. If you cancel outside these periods, you may be in breach of contract.
- The terms of the purchase agreement and any counter offers and addenda establish your rights and responsibilities.

YOU ARE STRONGLY ADVISED TO INVESTIGATE THE CONDITION AND SUITABILITY OF ALL ASPECTS OF THE PROPERTY. IF YOU DO NOT DO SO, YOU ARE ACTING AGAINST THE ADVICE OF BROKERS.

SELLER RIGHTS AND DUTIES:
- You have a duty to disclose material facts known to you that affect the value or desirability of the Property.
- You are obligated to make the Property available to the Buyer for inspections allowed by the contract.
- This form is not a substitute for completing a Real Estate Transfer Disclosure Statement, if required, and any other property-specific questionnaire or disclosure.
- The terms of the Purchase Agreement and any Counter Offers and Addenda establish your rights and responsibilities.

BROKER RIGHTS AND DUTIES:
- Brokers do not have expertise in all areas and matters affecting the Property or your evaluation of it.
- For most sales of residential properties with no more than four units, Brokers have a duty to make a reasonably competent and diligent visual inspection of the accessible areas of the Property and disclose to you material facts or defects that the inspection reveals.
- Many defects and conditions may not be discoverable by a Broker's visual inspection.
- If Broker gives a referral to another professional, Broker does not guarantee that person's performance. You may select any professional of your own choosing.
- Any written agreement between Broker and Buyer or Seller establishes the rights and responsibilities of those parties.

1. INSPECTIONS: Buyer and Seller are advised that Buyer has the right to obtain various inspections of the Property under most residential purchase agreements. Buyer is advised to have the Property inspected by a professional property inspection service within Buyer's inspection contingency period. A licensed building contractor or other professional may perform these services. The inspector generally does not look behind walls or under carpets, or take equipment apart. Certain items on the Property, such as chimneys and spark arresters, plumbing, heating, air conditioning, electrical wiring, pool and spa, septic system, well, roof, foundation and structural items may need to be inspected by another professional, such as a chimney sweep, plumber, electrician, pool and spa service, septic or well company or roofer. A general physical inspection typically will not test for mold, wood destroying pests, lead-based paint, radon, asbestos and other environmental hazards, geologic conditions, age, remaining useful life or water-tightness of roof, cracks, leaks or operational problems associated with a pool or spa or connection of the Property to a sewer system. If Buyer wants further information on any aspect of the Property, Broker recommends that Buyer have a discussion with the professional property inspector and that Buyer hire an appropriate professional for the area of concern to Buyer. Brokers do not have expertise in these areas. Brokers do not verify the results of any such inspection or guarantee the performance of any such inspector or service. Any election by Buyer to waive the right to a physical inspection of the Property or to rely on somebody other than an appropriate professional is against the advice of Brokers. Not all inspectors are licensed and licenses are not available for all types of inspection activities.

The copyright laws of the United States (Title 17 U.S. Code) forbid the unauthorized reproduction of this form, or any portion thereof, by photocopy machine or any other means, including facsimile or computerized formats. Copyright © 2004-2007, CALIFORNIA ASSOCIATION OF REALTORS®, INC. ALL RIGHTS RESERVED.

Buyer's Initials (_____)(_____)
Seller's Initials (_____)(_____)

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

2. SQUARE FOOTAGE, LOT SIZE AND BOUNDARIES: Buyer and Seller are advised that only an appraiser or land surveyor, as applicable, can reliably confirm square footage, lot size, Property corners and exact boundaries of the Property. Representations regarding these items that are made in a Multiple Listing Service, advertisements, and from property tax assessor records are often approximations, or based upon inaccurate or incomplete records. Fences, hedges, walls or other barriers may not represent actual boundary lines. Brokers have not verified any such representations. Brokers do not have expertise in this area. If Buyer wants information about the exact square footage, lot size or location of Property corners or boundaries, Broker recommends that Buyer hire an appraiser or licensed surveyor to investigate these matters during Buyer's inspection contingency period.

3. SOIL AND GEOLOGIC CONDITIONS: Buyer and Seller are advised that real estate in California is subject to settling, slippage, contraction, expansion, subsidence, earthquakes and other land movement. The Property may be constructed on fill or improperly compacted soil and may have inadequate drainage capability. Any of these matters can cause structural problems to improvements on the Property. Civil or geo-technical engineers are best suited to evaluate soil stability, grading, drainage and other soil conditions. Additionally, the Property may have known or unknown mines, mills, caves or wells. Brokers do not have expertise in this area. If Buyer wants further information, Broker recommends that Buyer hire an appropriate professional. Not all inspectors are licensed and licenses are not available for all types of inspections.

4. GEOLOGIC HAZARDS: Buyer and Seller are advised that California has experienced earthquakes in the past, and there is always a potential of future earthquakes. Damage caused by an earthquake may not be discoverable by Buyer's or Broker's visual inspection. Inspection by a licensed, qualified professional is strongly recommended to determine the structural integrity and safety of all structures and improvements on the Property. If the Property is a condominium, or located in a planned unit development or in a common interest subdivision, Buyer is advised to contact the homeowners association about earthquake repairs and retrofit work and the possibility of an increased or special assessment to defray the costs of earthquake repairs or retrofit work. Buyer is encouraged to obtain and read the booklet entitled "The Homeowners Guide to Earthquake Safety." In most cases a questionnaire within the booklet must be completed by Seller and the entire booklet given to the Buyer if the Property was built prior to 1960. If the Property was built before 1975, and contains structures constructed of masonry or precast (tilt up) concrete walls, with wood frame floors or roof, or if the building has unreinforced masonry walls, then Seller must provide Buyer a pamphlet entitled "The Commercial Property Owner's Guide to Earthquake Safety." Many areas have a wide range of geologic problems and numerous studies have been made of these conditions. Some of this information is available for public review at city and county planning departments. Buyer is encouraged to review the public maps and reports and/or obtain a geologist's inspection report. Brokers do not have expertise in this area. Buyer may be able to obtain earthquake insurance to protect their interest in the Property. Sellers who agree to provide financing should also consider requiring Buyers to obtain such insurance.

5. ENVIRONMENTAL HAZARDS: Buyer and Seller are advised that the presence of certain kinds of organisms, toxins and contaminants, including, but not limited to, mold (airborne, toxic or otherwise), fungi, mildew, lead-based paint and other lead contamination, asbestos, formaldehyde, radon, methane, other gases, fuel oil or chemical storage tanks, contaminated soil or water, hazardous waste, waste disposal sites, electromagnetic fields, nuclear sources, urea formaldehyde, or other materials may adversely affect the Property and the health of individuals who live on or work at the property as well as pets. If Buyer wants further information, Buyer is advised and Broker recommends that Buyer have the Property inspected for the existence of such conditions and organisms, and conditions that may lead to their formation. Not all inspectors are licensed and licenses are not available for all types of inspection activities. Buyer is also advised to consult with appropriate experts regarding this topic during Buyer's inspection contingency period. Brokers do not have expertise in this area. Broker recommends that Buyer and Seller read the booklets titled, "Residential Environmental Hazards: A Guide for Homeowners, Homebuyers, Landlords and Tenants," and "Protect Your Family From Lead In Your Home."

6. MOLD: Buyer and Seller are advised that the presence of certain kinds of mold, fungi, mildew and other organisms, sometimes referred to as "toxic mold" (collectively "Mold") may adversely affect the Property and the health of individuals who live on or work at the Property as well as pets. Mold does not affect all people the same way, and may not affect some people at all. Mold may be caused by water leaks or other sources of moisture such as, but not limited to, flooding, and leaks in windows, pipes and roof. Seller is advised to disclose the existence of any such conditions of which he or she is aware. Buyer should carefully review all of Seller's disclosures for any indication that any of these conditions exist. It is, however, possible that Mold may be hidden and that Seller is completely unaware of its existence. In addition, Mold is often undetectable from a visual inspection, a professional property inspection and even a structural pest control inspection. Brokers do not have expertise in this area. If Buyer wants further information, Broker recommends that Buyer have the Property tested for Mold by an environmental hygienist or other appropriate professional during Buyer's inspection contingency period. Not all inspectors are licensed and licenses are not available for all types of inspection activities.

Buyer's Initials (_____)(_____)
Seller's Initials (_____)(_____)

Reviewed by _____ Date _____

Copyright © 2004-2007, CALIFORNIA ASSOCIATION OF REALTORS®, INC.

7. WATER INTRUSION: Buyer and Seller are advised that many homes suffer from water intrusion or leakage. The causes of water intrusion are varied, and can include defective construction, faulty grading, deterioration of building materials and absence of waterproof barriers. Water intrusion can cause serious damage to the Property. This damage can consist of wood rot, mold, mildew and even damage to the structural integrity of the Property. The cost of repairing and remediating water intrusion damage and its causes can be very significant. The existence and cause of water intrusion is often difficult to detect. Because you, your Broker or a general home inspector cannot visually observe any effects of water intrusion, Buyer and Seller should not assume that such intrusion does not exist. Broker recommends that Buyer have the Property inspected for water intrusion by an appropriate professional. Brokers do not have expertise in this area.

8. SEPTIC SYSTEM(S): Buyer and Seller are advised that a property may be served by one or more septic systems even though adjoining properties are connected to a sewer line. Buyer and Seller are also advised that some septic tanks and systems may have been abandoned or have leaked into ground water sources. Buyer is advised to contact the appropriate government agency to verify that the Property is connected to a sewer or served by a septic system. If the Property is served by a septic system it may consist of a septic tank, cesspool, pits, leach lines or a combination of such mechanisms ("collectively, System"). No representation or warranty is made by Seller or Broker concerning the condition, operability, size, capacity or future expansion of a System, nor whether a System is adequate for use by the intended occupants of the Property. A change in the number of occupants or the quantity, composition or methods of depositing waste may affect the efficiency of the System. In addition, the amount of rainfall and ground water table may also affect the efficiency of the System. Many factors including, but not limited to, natural forces, age, deterioration of materials and the load imposed on a System can cause the System to fail at any time. Broker recommends that Buyer obtain an independent evaluation of any System by a qualified sanitation professional during Buyer's inspection contingency period. Brokers do not have expertise in this area. Buyer should consult with their sanitation professional to determine if their report includes the tank only, or other additional components of the System such as pits and leach fields. Not all inspectors are licensed and licenses are not available for all types of inspection activities. In some cases, Buyer's lender as well as local government agencies may require System inspection. System-related maintenance costs may include, but not be limited to, locating, pumping or providing outlets to ground level. Brokers are unable to advise Buyer or Seller regarding System-related issues or associated costs, which may be significant. If Buyer and Seller agree to obtain a System inspection, Buyer and Seller are cautioned that the inspection cost may include, but not be limited to, the costs of locating, pumping or providing outlets to ground level.

9. WELL AND WATER SYSTEM(S): Buyer and Seller are advised that the Property may be served by one or more water wells, springs, or private community or public water systems. Any of these private or public water systems may contain bacteria, chemicals, minerals and metals, such as chromium. Well(s) may have been abandoned on the Property. Buyer is advised to have both the quality and the quantity of water evaluated, and to obtain an analysis of the quality of any domestic and agricultural water in use, or to be used at the Property, from whatever source. Water quality tests can include not only tests for bacteria, such as coliform, but also tests for organic and inorganic chemicals, metals, mineral content and gross alpha testing for radioactivity. Broker recommends that Buyer consult with a licensed, qualified well and pump company and local government agency to determine whether any well/spring or water system will adequately serve Buyer's intended use and that Buyer have a well consultant perform an extended well output test for this purpose. Water well or spring capacity, quantity output and quality may change at any time. There are no guarantees as to the future water quality, quantity or duration of any well or spring. If Buyer wants further information, Broker recommends that Buyer obtain an inspection of the condition, age, adequacy and performance of all components of the well/spring and any water system during Buyer's inspection contingency period. Brokers do not have expertise in this area.

10. WOOD DESTROYING PESTS: Buyer and Seller are advised that the presence of, or conditions likely to lead to the presence of, or other infestation or infection of wood destroying pests and organisms may adversely affect the Property. Inspection reports covering these items can be separated into two sections: Section 1 identifies areas where infestation or infection is evident. Section 2 identifies areas where there are conditions likely to lead to infestation or infection. Brokers do not have expertise in this area. If Buyer wants further information, Buyer is advised and Broker recommends that Buyer have the Property inspected for the existence of such conditions and organisms, and conditions that may lead to their formation by a registered structural pest control company during Buyer's inspection contingency period.

11. EASEMENTS, ACCESS AND ENCROACHMENTS: Buyer and Seller are advised that confirming the exact location of easements, shared or private driveways or roadways, and encroachments on or to the Property may be possible only by conducting a survey. There may be unrecorded easements, access rights, encroachments and other agreements affecting the Property that may not be disclosed by a survey. Representations regarding these items that are made in a Multiple Listing Service, advertisements, or plotted by a title company are often approximations, or based upon inaccurate or incomplete records. Brokers have not verified any such representations. If Buyer wants further information Buyer is advised and Broker recommends that Buyer hire a licensed surveyor during Buyer's inspection contingency period. Brokers do not have expertise in this area.

Buyer's Initials (_____)(_____)
Seller's Initials (_____)(_____)

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

Copyright © 2004-2007, CALIFORNIA ASSOCIATION OF REALTORS®, INC.

12. EARTHQUAKE FAULT ZONES AND SEISMIC HAZARD ZONES: Buyer and Seller are advised that California Public Resources Code Sections 2622 and 2696 require the delineation and mapping of "Earthquake Fault Zones" along known active faults and "Seismic Hazard Zones" in California. Affected cities and counties must regulate certain development projects within these zones. Construction or development on affected properties may be subject to the findings of a geological report prepared by a registered California geologist. Generally, Seller must disclose if the Property is in such a zone and can use a research company to aid in the process. If Buyer wants further information, Broker recommends that, during Buyer's inspection contingency period, Buyer make independent inquiries with such research companies or with appropriate government agencies concerning the use and improvement of the Property. Brokers do not have expertise in this area. Buyer is advised that there is a potential for earthquakes and seismic hazards even outside designated zones.

13. FIRE HAZARDS: Buyer and Seller are advised that fires annually cause the destruction of thousands of homes. Due to varied climate and topography, certain areas have higher risks of fires than others. Certain types of materials used in home construction create a greater risk of fire than others. If the Property is located within a State Fire Responsibility Area or a Very High Fire Hazard Zone, generally Seller must disclose that fact to Buyer under California Public Resources Code Section 4136 and California Government Code Sections 51178 and 51183.5, and may use a research company to aid in the process. If Buyer wants further information Broker recommends that, during Buyer's inspection contingency period, Buyer contact the local fire department and Buyer's insurance agent regarding the risk of fire. Brokers do not have expertise in this area. Buyer is advised that there is a potential for fires even outside designated zones.

14. FLOOD HAZARDS: Buyer and Seller are advised that if the Property is located within a Special Flood Hazard Area, as designated by the Federal Emergency Management Agency, or an area of Potential Flooding pursuant to California Government Code Section 8589.3, generally Seller must disclose this fact to Buyer and may use a research company to aid in the process. The National Flood Insurance Program was established to identify all flood plain areas and establish flood-risk zones within those areas. The program mandates flood insurance for properties within high-risk zones if loans are obtained from a federally-regulated financial institution or are insured by any agency of the United States Government. The extent of coverage and costs may vary. If Buyer wants further information, Broker recommends that Buyer consult his or her lender and/or insurance agent during Buyer's inspection contingency period. Brokers do not have expertise in this area. Buyer is advised that there is a potential for flooding even outside designated zones.

15. BUILDING PERMITS, ZONING AND CODE COMPLIANCE: Buyer and Seller are advised that any structure on the Property, including the original structure and any addition, modification, remodel or improvement may have been built without permits, not according to building codes, or in violation of zoning laws. Further, even if such structure was built according to the then-existing code or zoning requirement, it may not be in compliance with current building standards or local zoning. It is also possible that local law may not permit structures that now exist to be rebuilt in the event of damage or destruction. Buyer is advised to check with appropriate government agencies or third party professionals to verify permits and legal requirements and the effect of such requirements on current and future use of the Property, its development and size. If Buyer wants further information Broker recommends that Buyer discuss the issue with an appropriate professional during Buyer's inspection contingency period. Brokers do not have expertise in this area.

16. VIEWS: Buyer and Seller are advised that present views from the Property may be affected by future development or growth of trees and vegetation on adjacent properties and any other property within the line of sight of the Property. Broker makes no representation regarding the preservation of existing views. If Buyer wants further information, Broker recommends that Buyer review Covenants, Conditions and Restrictions, if any, and contact neighboring property owners, government agencies and homeowner associations, if any, during Buyer's inspection contingency period. Brokers do not have expertise in this area.

17. FUTURE REPAIRS, REPLACEMENTS AND REMODELS: Buyer and Seller are advised that replacement or repairs of certain systems or remodels of portions of the Property may trigger requirements that homeowners comply with laws and regulations that either come into effect after Close of Escrow or are not required to be complied with until the replacement, repair or remodel has occurred. Permit or code requirements or building standards may change after Close of Escrow, resulting in increasing costs to repair existing features. In particular, changes to state and federal energy efficiency regulations impact the installation, replacement and some repairs of heating and air conditioning units (HVAC). Federal regulations now require manufacturers of HVAC units to produce only units meeting a new higher Seasonal Energy Efficiency Rating (SEER). This will likely impact repairs and replacements of existing HVAC units. State regulations now require that when installing or replacing HVAC units, with some exceptions, duct work must be tested for leaks. Duct work leaking more than 15 percent must be repaired to reduce leaks. The average existing duct work typically leaks 30 percent. More information is available at the California Energy Commission's website http://www.energy.ca.gov/title24/changeout. Home warranty policies may not cover such inspections or repairs. If Buyer wants further information Broker recommends that Buyer discuss the issue with an appropriate professional during Buyer's inspection contingency period. Brokers do not have expertise in this area.

18. ERRANT GOLF BALLS: Buyer and Seller are advised that if the Property is located adjacent to or near a golf course there is a possibility that golf balls may damage the Property or injure persons or pets on it. Additionally, persons playing golf may enter the Property to retrieve errant golf balls or for other purposes. Broker recommends that Buyer investigate this possibility during Buyer's Inspection contingency period. Brokers do not have expertise in this area.

Buyer's Initials (_____)(_____)
Seller's Initials (_____)(_____)

Copyright © 2004-2007, CALIFORNIA ASSOCIATION OF REALTORS®, INC.

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

STATEWIDE BUYER AND SELLER ADVISORY (SBSA PAGE 4 OF 10)

Print

19. SCHOOLS: Buyer and Seller are advised that children living in the Property may not, for numerous reasons, be permitted to attend the school nearest the Property. Various factors including, but not limited to, open enrollment policies, busing, overcrowding and class size reductions may affect which public school serves the Property. School district boundaries are subject to change. Buyer is advised to verify whether the Property is now, and at the Close of Escrow will be, in the school district Buyer understands it to be in and whether residing in the Property entitles a person to attend any specific school that Buyer is interested in. Broker recommends that Buyer contact the local school or school district for additional information during Buyer's inspection contingency period. Brokers do not have expertise in this area.

20. NEIGHBORHOOD NOISE SOURCES: Buyer and Seller are advised that even if the Property is not in an identified airport noise influence area the Property may still be subject to airplanes and other aircraft, commercial or military or both, flying overhead. Other common sources of noise include traffic on streets and highways, trains and general neighborhood noise from people, dogs and other animals. Noise levels and types of noise that bother one person may be acceptable to others. Buyer is advised to satisfy him/herself with regard to any sources of and amounts of noise at different times of day and night. Brokers do not have expertise in this area.

21. PETS AND ANIMALS: Buyer and Seller are advised that the current or previous owner(s) may have had domesticated or other pets and animals at the Property. Odors from animal urine contamination may be dormant for long periods of time and then become active because of heat, humidity or other factors and may not be eliminated by cleaning or replacing carpets or other cleaning. Pet urine and feces can also damage hardwood floors and other floor coverings. Additionally, an animal may have had fleas, ticks and other pests that remain on the Property after the animal has been removed. If Buyer wants further information, Broker recommends that Buyer discuss the issue with an appropriate professional during Buyer's inspection contingency period. Brokers do not have expertise in this area.

22. SECURITY AND SAFETY: Buyer and Seller are advised that state and local Law may require the installation of barriers, access alarms, self-latching mechanisms and/or other measures to decrease the risk to children and other persons of existing swimming pools and hot tubs, as well as various fire safety and other measures concerning other features of the Property. Compliance requirements differ from city to city and county to county. Unless specifically agreed, the Property may not be in compliance with these requirements. Brokers do not have expertise in this area. If Buyer wants further information, Broker recommends that Buyer contact local government agencies about these restrictions and other requirements.

23. RETROFIT: Buyer and Seller are advised that state and local Law may require the installation of operable smoke detectors, bracing or strapping of water heaters, and completion of a corresponding written statement of compliance that is delivered to Buyer. Some city and county governments may impose additional retrofit standards, including, but not limited to, installing low-flow toilets and showerheads, gas shut-off valves, and tempered glass. Brokers do not have expertise in this area. Broker recommends that Buyer and Seller consult with the appropriate government agencies, inspectors, and other professionals to determine the retrofit standards for the Property, the extent to which the Property complies with such standards, and the costs, if any, of compliance.

24. WATER SHORTAGES AND CONSERVATION: Buyer and Seller are advised that the Property may be located in an area that could experience water shortages. The policies of local water districts and the city or county in which the Property is located can result in the occurrence of any or all of the following: **(i)** limitations on the amount of water available to the Property, **(ii)** restrictions on the use of water, and **(iii)** an increasingly graduated cost per unit of water use, including, but not limited to, penalties for excess usage. For further information, Broker recommends that Buyer contact the supplier of water to the Property regarding the supplier's current or anticipated policies on water usage and to determine the extent to which those policies may affect Buyer's intended use of the Property. If the Property is serviced by a private well, Buyer is advised that drought conditions and/or a low water table may make it necessary to arrange, through a private supplier, for delivery of water to the Property. Buyers should contact water truck companies for the costs involved. Brokers do not have expertise in this area.

25. NEIGHBORHOOD, AREA; PERSONAL FACTORS: Buyer and Seller are advised that the following may affect the Property or Buyer's intended use of it: neighborhood or area conditions, including schools, proximity and adequacy of law enforcement, crime, fire protection, other government services, availability, adequacy and cost of any speed-wired, wireless internet connections or other telecommunications or other technology services and installations, proximity to manufacturing, commercial, industrial, airport or agricultural activities or military ordnance locations, existing and proposed transportation, construction, and development, any other source that may affect noise, view, traffic, or odor, wild and domestic animals, other nuisances, hazards, or circumstances, protected species, wetland properties, botanical diseases, historic or other governmentally-protected sites or improvements, cemeteries, conditions and influences of significance to certain cultures and/or religions, and personal needs, requirements and preferences of Buyer.

Buyer's Initials (_____)(_____)
Seller's Initials (_____)(_____)

Copyright © 2004-2007, CALIFORNIA ASSOCIATION OF REALTORS®, INC.

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

STATEWIDE BUYER AND SELLER ADVISORY (SBSA PAGE 5 OF 10)

Print

26. INSURANCE: Buyer and Seller are advised that Buyer may have difficulty obtaining insurance regarding the Property if there has been a prior insurance claim affecting the Property or made by Buyer but unrelated to the Property. Seller is required by C.A.R. Form RPA to disclose known insurance claims made during the past five years. Sellers may not be aware of claims prior to their ownership. If Buyer wants further information, Broker recommends that, during Buyer's inspection contingency period, Buyer conduct his or her own investigation for past claims. Buyer may need to obtain Seller's consent in order to have access to certain investigation reports. If the Property is a condominium, or is located in a planned unit development or other common interest subdivision, Buyer and Seller are advised to determine if the individual unit is covered by the Homeowner Association Insurance. Broker recommends that Buyer consult Buyer's insurance agents during Buyer's inspection contingency period to determine the need, availability and possibility of securing any and all forms of other insurance or coverage or any conditions imposed by insurer as a requirement of issuing insurance. If Buyer takes possession prior to Close of Escrow or Seller remains in possession after Close of Escrow, whether for a limited or extended period of time, Broker recommends that Buyer and Seller each consult with their own insurance agent regarding insurance or coverage that could protect them in the transaction (including but not limited to: personal property, flood, earthquake, umbrella and renter's). Brokers do not have expertise in this area.

27. CALIFORNIA FAIR PLAN: Buyer and Seller are advised that insurance for certain hillside, oceanfront and brush properties may be available only from the California Fair Plan. This may increase the cost of insurance for such properties and coverage may be limited. Broker recommends that Buyer consult with Buyer's own insurance agent during Buyer's inspection contingency period regarding the availability of coverage under the California Fair Plan and the length of time it may take for processing of a California Fair Plan application. Brokers do not have expertise in this area.

28. HISTORICAL DESIGNATION, COASTAL COMMISSION, ARCHITECTURAL, LANDSCAPE, AGRICULTURAL OR OPEN SPACE AND OTHER RESTRICTIONS ON BUILDINGS OR IMPROVEMENTS: Buyer and Seller are advised that the Property may be: **(i)** designated as a historical landmark, **(ii)** protected by a historical conservancy, **(iii)** subject to an architectural or landscaping review process, **(iv)** within the jurisdiction of the California Coastal Commission or other government agency, or **(v)** subject to a contract preserving use of all or part of the Property for agriculture or open space. If the Property is so designated or within the jurisdiction of any such, or similar, government agency then there may be restrictions on Buyer's ability to develop, remove or trim trees or other landscaping, remodel, make improvements to and build on or rebuild the Property. Broker recommends that Buyer satisfy him/herself during Buyer's inspection contingency period if any of these issues are of concern to Buyer. Brokers do not have expertise in this area.

29. 1915 BOND AND MELLO-ROOS COMMUNITY AND OTHER FACILITIES DISTRICTS: Buyer and Seller are advised that the Property may be subject to an improvement bond assessment under the Improvement Bond Act of 1915 and/or a levy of a special tax pursuant to a Mello-Roos community facilities or other district. Seller is generally required to make a good faith effort to obtain a disclosure notice from any local agency collecting such taxes and deliver such notice to Buyers. Brokers do not have expertise in this area.

30. HOMEOWNER ASSOCIATIONS AND COVENANTS, CONDITIONS AND RESTRICTIONS (CC&Rs): Buyer and Seller are advised that if the Property is a condominium, or located in a planned unit development, or in a common interest subdivision there are typically restrictions on use of the Property and rules that must be followed. Restrictions and rules are commonly found in Declarations of Covenants, Conditions and Restrictions (CC&Rs) and other governing documents. Further there is likely to be a homeowner association (HOA) that has the authority to affect the Property and its use. Whether or not there is a HOA, the Property may still be subject to CC&Rs restricting use of the Property. The HOA typically has the authority to enforce the rules of the association, assess monetary payments (both regular monthly dues and special assessments) to provide for the upkeep and maintenance of the common areas, and enforce the rules and assessment obligations. If you fail to abide by the rules or pay monies owed to the HOA, the HOA may put a lien against your Property. The law requires the Seller to provide the Buyer with the CC&Rs and other governing documents, as well as a copy of the HOA's current financial statement and operating budget, among other documents. Buyer is advised to carefully review all HOA documents provided by Seller and the CC&Rs, if any, and satisfy him/herself regarding the use and restrictions of the Property, the amount of monthly dues and/or assessments, the adequacy of reserves, current and past insurance coverage and claims and the possibility of any legal action that may be taken by or against the HOA. The HOA may not have insurance or may not cover personal property belonging to the owner of the unit in the condominium, common interest or planned unit development. See paragraph 26 for further information regarding insurance. Brokers do not have expertise in this area.

31. COMMUNITY ENHANCEMENT AND PRIVATE TRANSFER FEES: Buyer and Seller are advised that some areas or communities may have enhancement fees or user-type fees, or private transfer fees, over and above any stated association fees. Private transfer fees: (A) may last for a fixed period of time or in perpetuity, (B) are typically calculated as a percentage of home's sales price, and (C) may have private parties, charitable organizations or interest-based groups as their recipients. Brokers do not have expertise in this area.

Buyer's Initials (_____)(_____)
Seller's Initials (_____)(_____)

Copyright © 2004-2007, CALIFORNIA ASSOCIATION OF REALTORS®, INC.

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

Print

32. GENERAL RECALL/DEFECTIVE PRODUCT/CLASS ACTION INFORMATION: Buyer and Seller are advised that government entities and manufacturers may at any time issue recall notices and/or warnings about products that may be present in the Property, and that these notices or warnings can change. There is no single, all-inclusive source of information on product recalls, defective products or class actions; however, the U.S. Consumer Product Safety Commission (CPSC) maintains a website that contains useful information. If Buyer wants further information regarding the items listed below, Broker recommends that Buyer consult the CPSC website at http://www.cpsc.gov during Buyer's inspection contingency period. The following are examples of recall/defective products/class action information. The information is not exclusive. If Buyer wants further information, Broker recommends that Buyer contact the sources below. Brokers do not have expertise in this area and will not determine if any aspect of the Property is subject to a recall or is affected by a class action lawsuit. (NOTE: While the information below is believed to be current as of the revision date of this form, phone numbers and web addresses may change or be discontinued.)

A. FURNACES: Buyer is advised that the CPSC has issued a warning regarding certain gas-fired horizontal forced-air furnaces that present a substantial risk of fire. The furnaces in question were manufactured from 1983 to 1994 by Consolidated Industries and were marketed under many different brand names. Homes built before 1983 or after 1994 could still have the furnaces in question due to replacements or remodeling. If Buyer wants further information, Broker recommends that Buyer contact CPSC's hotline at (800) 638-2772.

B. WHIRLPOOL MICROWAVE-HOOD COMBINATION: Buyer is advised that Whirlpool Corporation has voluntarily recalled approximately 1.8 million microwave-hood combinations that have been known to overheat and catch fire. The units at issue are installed above ranges and are sold under the Whirlpool, KitchenAid and Kenmore brand names. If Buyer wants further information, Broker recommends that Buyer contact Whirlpool by phone at (800) 785-8897 or at its website, http://www.repair.whirlpool.com.

C. ROOF TILES: Buyer is advised that there is a class action lawsuit concerning certain fire free tiles and quantum panels manufactured and installed by RE-Con Building Products, Inc. from December 1993 to November 1997. If Buyer wants further information, Broker recommends that Buyer call (800) 966-3696 or view the website at http://www.firefreeclaims.com.

D. FIRE SPRINKLER: Buyer is advised that Central Sprinkler Company is recalling 35 million fire sprinkler heads that may be defective. If Buyer wants further information, Broker recommends that Buyer consult the CPSC website at http://www.cpsc.gov or Central Sprinkler Company at (866) 505-8553 or http://www.sprinklerreplacement.com.

E. WATER HEATER: Buyer is advised that certain water heaters manufactured by a variety of companies between 1993 and 1997 may be defective. If Buyer wants further information, Broker recommends that Buyer discuss the issue with an appropriate professional who can determine if the water heater on the Property is defective.

F. ALUMINUM WIRING: Buyer is advised that some properties in California are wired in whole or in part with aluminum wiring which was approved at the time of construction but subsequently determined to be a potential hazard. If Buyer wants further information, Broker recommends that Buyer discuss the issue with an appropriate professional who can determine if the wiring on the Property is defective.

G. GALVANIZED, ABS, POLYBUTELENE AND COPPER PIPE: Buyer is advised that galvanized steel water pipes may corrode and leak after several years and that ABS plastic drain waste and vent pipe may be subject to failure. Buyer is also advised that the adhesive used in the installation of polybutelene pipe has been subject to failure. Additionally, copper pipe installed in slabs may develop leaks as result of reaction to certain soils. If Buyer wants further information, Broker recommends that Buyer discuss the issue with an appropriate professional who can determine if the water pipes and drains on the Property are defective.

H. WATER HEATER GAS CONTROL VALVES: Buyer is advised that the CPSC in cooperation with Robertshaw Controls Company has announced a voluntary recall of approximately 178,000 gas control valves installed on water heaters manufactured between July 2005 and August 2005 with production date codes 5-31 through and

including 5-33 under brand names American Proline, Bradford White, GE, GSE, Hotpoint, Jetglas, John Wood, Lochinvar, Premire Plus, Powerflex, Rheem, Richmond, Ruud, Vanguard, Whirlpool and U.S. Craftsman. The CPSC reports that the screws on the valves could break allowing gas to escape from the valves. If Buyer wants further information, Broker recommends that Buyer consult the CPSC website at http://www.cpsc.gov or contact Robertshaw Controls at (888) 225-1071 or http://www.robertshaw.com.

SAMPLE

Copyright © 2004-2007, CALIFORNIA ASSOCIATION OF REALTORS®, INC.

I. ARC-FAULT CIRCUIT BREAKER: Buyer is advised that the CPSC in cooperation with Schneider Electric has announced a voluntary recall of approximately 700,000 Square D Q® and Homeline® AFCI circuit breakers manufactured by Schneider Electric North American Operating Division. The recalled arc-fault interrupter circuit breakers are designed for use in 15 and 20-amp branch circuits; have a blue test button and were manufactured between March 2004 and September 2004. Tests show that these circuit breakers may not provide the arc-fault protection required by the 2001 California Electrical Code, Section 210-21. If Buyer wants further information, Broker recommends that Buyer consult the CPSC website at http://www.cpsc.gov or contact Schneider Electric at (877) 202-9064 or http://www.us.squared.com/recallafci.

33. RENTAL PROPERTY RESTRICTIONS: Buyer and Seller are advised that some cities and counties impose restrictions that limit the rent that can be charged to a tenant, the maximum number of tenants who can occupy the property and the right of a landlord to terminate a tenancy and the costs to do so. If Buyer wants further information, Broker recommends that Buyer investigate the issue with an appropriate government authority during Buyer's inspection contingency period. Brokers do not have expertise in this area.

34. LAND LEASE: Buyer and Seller are advised that certain developments are built on leased land. This means that: (i) Buyer does not own the land, (ii) the right to occupy the land will terminate at some time, (iii) the cost to lease the land may increase at some point in the future, and (iv) Buyer may not be able to obtain title insurance. If Buyer wants further information, Broker recommends that Buyer discuss the issue with an attorney or other appropriate professional. Brokers do not have expertise in this area.

35. HOME WARRANTY: Buyer and Seller are advised that Buyer and Seller can purchase home warranty plans covering certain standard systems of the Property both before and after Close of Escrow. Seller can obtain coverage for the Property during the listing period. For an additional premium, an upgraded policy providing additional coverage for air conditioning, pool and spa and other features can be purchased. Home warranties do not cover every aspect of the Property and may not cover inspections or upgrades for repairs required by state or federal laws. Broker recommends that Buyer review the policy for details. Brokers do not have expertise in this area.

36. INTERNET ADVERTISING: Buyer and Seller are advised that Broker may employ a service to provide a "virtual tour" or Internet marketing of the Property, permitting potential buyers to view the Property over the Internet. Neither the service provider nor Broker has control over who will obtain access to the service or what action such persons might take. Buyer and Seller are advised that Brokers have no control over how long the information concerning the Property will be available on the Internet. Brokers do not have expertise in this area.

37. ESCROW FUNDS: Buyer and Seller are advised that California Insurance Code Section 12413.1 provides that escrow companies cannot disburse funds unless there are sufficient "good funds" to cover the disbursement. "Good funds" are defined as cash, wire transfers and cashiers' or certified checks drawn on California depositories. Escrow companies vary in their definitions of "good funds." Broker recommends that Buyer and Seller ask the escrow company regarding its treatment of "good funds." All drafts and out-of-state checks are subject to waiting periods and do not constitute "good funds" until the money is physically transferred to the escrow holder's account. Brokers do not have expertise in this area.

38. NOTICE OF YOUR "SUPPLEMENTAL" PROPERTY TAX BILL: Buyer and Seller are advised that pursuant to Civil Code § 1102.6(c), Seller or his or her agent is required to provide the following "Notice of Your 'Supplemental' Property Tax Bill" to the Buyer:

"California property tax law requires the Assessor to revalue real property at the time the ownership of property changes. Because of this law, you may receive one or two supplemental tax bills, depending on when your loan closes.

The supplemental tax bills are not mailed to your lender. If you have arranged for your property tax payments to be paid through an impound account, the supplemental tax bills will not be paid by your lender. It is your responsibility to pay these supplemental bills directly to the Tax Collector.
If you have any questions concerning this matter, please call your Tax Collector's Office."

Although the notice refers to loan closing as a trigger, it is actually the change of ownership which triggers this reassessment. Therefore, the Property can be reassessed even if there is no loan involved in the purchase of the Property. The purchase agreement may allocate supplemental tax bills received after the Close of Escrow to the Buyer. If Buyer wants further information concerning these matters, Broker recommends that Buyer discuss the issue with the County Assessor or Tax Collector. Brokers do not have expertise in this area.

Buyer's Initials (_____)(_____)
Seller's Initials (_____)(_____)

Reviewed by _____ Date _____

Copyright © 2004-2007, CALIFORNIA ASSOCIATION OF REALTORS®, INC.

Print

39. NON CONFIDENTIALITY OF OFFERS: Buyer is advised that Seller or Listing Agent may disclose the existence, terms, or conditions of Buyer's offer unless all parties and their agent have signed a written confidentiality agreement. Whether any such information is actually disclosed depends on many factors, such as current market conditions, the prevailing practice in the real estate community, the Listing Agent's marketing strategy and the instructions of the Seller.

40. FIRPTA/CALIFORNIA WITHHOLDING: Buyer and Seller are advised that: (i) Internal Revenue Code Section 1445 requires a Buyer to withhold and remit to the Internal Revenue Service 10% of the purchase price if Seller is a non-resident alien, unless an exemption applies. Seller may avoid withholding by providing Buyer a statement of non-foreign status. The statement must be signed by Seller under penalty of perjury and include Seller's tax identification number. Buyer can also avoid the federal withholding requirement if the property price is $300,000 or less, and the Buyer signs an affidavit stating Buyer intends to occupy the property as a principal residence. (ii) California Revenue and Taxation Code Section 18662 requires that a Buyer withhold and remit to the California Franchise Tax Board 3 1/3% of the purchase price unless the Seller signs an affidavit that the property was the Seller's (or the decedent's if a trust or probate sale) principal residence or that the sales price is $100,000 or less or another exemption applies. Exemptions from withholding also apply to legal entities such as corporations, LLCs, and partnerships. Brokers cannot give tax advice. Broker recommends that Buyer and Seller seek advice from a CPA, attorney or taxing authority. Brokers do not have expertise in this area.

41. LIQUIDATED DAMAGES: Buyer and Seller are advised that a liquidated damages clause is a provision Buyer and Seller can use to agree in advance to the amount of damages that a seller will receive if a buyer breaches the agreement. The clause usually provides that a seller will retain a Buyer's initial deposit paid if the Buyer breaches the agreement, and generally must be separately initialed by both parties to be enforceable. For any additional deposits to be covered by the liquidated damages clause, there generally must be another separately signed or initialed agreement. However, if the Property contains from 1 to 4 units, one of which the Buyer intends to occupy, California Civil Code Section 1675 limits the amount of the deposit subject to liquidated damages to 3% of the purchase price. Even though both parties have agreed to a liquidated damages clause, an escrow company will usually require either a judge's or arbitrator's decision or instructions signed by both parties in order to release the Buyer's deposit to the Seller. Buyers and Sellers must decide on their own, or with the advice of legal counsel, whether to agree to a liquidated damages clause. Brokers do not have expertise in this area.

42. MEDIATION: Buyer and Seller are advised that mediation is a process by which the parties hire a neutral person to facilitate discussion and negotiation between the parties with the goal of helping them reach a settlement of their dispute. The parties generally share in the cost of this confidential, non-binding negotiation. If no agreement is reached, either party can pursue further legal action. Under C.A.R. Form RPA-CA; (i) the parties must mediate any dispute arising out of their agreement (with a few limited exceptions, such as matters within the jurisdiction of a small claims court) before they resort to arbitration or court, and (ii) if a party proceeds to arbitration or court without first attempting to mediate the dispute, that party risks losing the right to recover attorney fees even if he or she prevails.

43. ARBITRATION: Buyer and Seller are advised that arbitration is a process by which the disputing parties hire a neutral person to render a decision. Generally, arbitration is faster and less expensive than resolving disputes by litigating in court. The rules are usually less formal than in court, and it is a private process not on the public record. By agreeing to arbitration the parties give up the right to a jury trial and to appeal. Arbitration decisions have been upheld even when arbitrators have made a mistake as to the law or the facts. If the parties agree to arbitration, then any dispute arising out of their agreement (with a few limited exceptions) must be submitted to binding arbitration. Buyer and Seller must weigh the benefits of a potentially quicker and less expensive arbitration against giving up the right to a jury trial and the right to appeal. Brokers cannot give legal advice regarding these matters. Buyers and Sellers must decide on their own, or with the advice of legal counsel, whether to agree to arbitration. Brokers do not have expertise in this area.

Buyer's Initials (_____)(_____)
Seller's Initials (_____)(_____)

Reviewed by _____ Date _____

Copyright © 2004-2007, CALIFORNIA ASSOCIATION OF REALTORS®, INC.

Print

Property Address: _____ Date: _____

44. LOCAL ADDENDA (IF CHECKED):

The following local disclosures or addenda are attached:

A. ☐ _____

B. ☐ _____

C. ☐ _____

D. ☐ _____

Buyer and Seller acknowledge and agree that Broker: **(i)** does not decide what price Buyer should pay or Seller should accept; **(ii)** does not guarantee the condition of the Property; **(iii)** does not guarantee the performance, adequacy or completeness of inspections, services, products or repairs provided or made by Seller or others; **(iv)** does not have an obligation to conduct an inspection of common areas or areas off the site of the Property **(v)** shall not be responsible for identifying defects on the Property, in common areas, or offsite unless such defects are visually observable by an inspection of reasonably accessible areas of the Property or are known to Broker; **(vi)** shall not be responsible for inspecting public records or permits concerning the title or use of Property; **(vii)** shall not be responsible for identifying the location of boundary lines or other items affecting title; **(viii)** shall not be responsible for verifying square footage, representations of others or information contained in investigation reports, Multiple Listing Service, advertisements, flyers or other promotional material; **(ix)** shall not be responsible for providing legal or tax advice regarding any aspect of a transaction entered into by Buyer or Seller; and **(x)** shall not be responsible for providing other advice or information that exceeds the knowledge, education and experience required to perform real estate licensed activity. Buyer and Seller agree to seek legal, tax, insurance, title and other desired assistance from appropriate professionals.

By signing below, Buyer and Seller acknowledge that each has read, understands and received a copy of this Advisory. Buyer and Seller are encouraged to read it carefully.

Date _____ Date _____

BUYER _____ BUYER _____

_____ _____

(Print name) (Print name)

_____ _____

(Address)

Date _____ Date _____

SELLER _____ SELLER _____

_____ _____

(Print name) (Print name)

_____

(Address)

Real Estate Broker (Selling Firm) _____ DRE Lic. # _____

By _____ DRE Lic. # _____ Date _____

Address _____ City _____ State _____ Zip _____

Telephone _____ Fax _____ E-mail _____

Real Estate Broker (Listing Firm) _____ DRE Lic. # _____

By _____ DRE Lic. # _____ Date _____

Address _____ City _____ State _____ Zip _____

Telephone _____ Fax _____ E-mail _____

THIS FORM HAS BEEN APPROVED BY THE CALIFORNIA ASSOCIATION OF REALTORS® (C.A.R.). NO REPRESENTATION IS MADE AS TO THE LEGAL VALIDITY OR ADEQUACY OF ANY PROVISION IN ANY SPECIFIC TRANSACTION. A REAL ESTATE BROKER IS THE PERSON QUALIFIED TO ADVISE ON REAL ESTATE TRANSACTIONS. IF YOU DESIRE LEGAL OR TAX ADVICE, CONSULT AN APPROPRIATE PROFESSIONAL.
This form is available for use by the entire real estate industry. It is not intended to identify the user as a REALTOR®. REALTOR® is a registered collective membership mark which may be used only by members of the NATIONAL ASSOCIATION OF REALTORS® who subscribe to its Code of Ethics.

Published and Distributed by:
REAL ESTATE BUSINESS SERVICES, INC.
a subsidiary of the California Association of REALTORS®
525 South Virgil Avenue, Los Angeles, California 90020

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

STATEWIDE BUYER AND SELLER ADVISORY (SBSA PAGE 10 OF 10)

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/6 Residential Purchase and Sale Transactions/ §6.28 5. Form: Notice to Buyer to Perform (CAR Form NBP)

§6.28 5. Form: Notice to Buyer to Perform (CAR Form NBP)

Print

CALIFORNIA ASSOCIATION OF REALTORS®

NOTICE TO BUYER TO PERFORM
No. _____
(C.A.R. Form NBP, Revised 04/09)

In accordance with the terms and conditions of the ☐ California Residential Purchase Agreement (C.A.R. Form RPA) or ☐ Residential Income Property Purchase Agreement (C.A.R. Form RIPA), or ☐ Commercial Property Purchase Agreement (C.A.R. Form CPA), or ☐ Vacant Land Purchase Agreement (C.A.R. Form VLPA),or ☐ Other _____ ("Agreement"), dated _____, on property known as _____ _____ ("Property"), between _____ ("Buyer"), and _____ ("Seller").

SELLER hereby gives Buyer notice to remove the following contingencies or take the specified contractual action:

I. Contingency

☐ **ALL CONTINGENCIES**

A. ☐ Loan (Paragraph 2I)
B. ☐ Appraisal (Paragraph 2J)
C. ☐ Tenant-Occupied Property (Paragraph 3C(iii))
D. ☐ Disclosures/Reports (Paragraphs 4 and 5)
E. ☐ Common Interest (HOA or OA) Disclosures (Paragraph 6B)
F. ☐ Buyer Investigation, including insurability (Paragraph 9)
G. ☐ Title: Preliminary Report (Paragraph 12)
H. ☐ Sale of Buyer's Property (Paragraph 13)
I. ☐ _____
J. ☐ _____
K. ☐ _____

II. Contractual Action

L. ☐ Initial Deposit (Paragraph 2A)
M. ☐ Increased Deposit (Paragraph 2B)
N. ☐ Loan Application Letter (Paragraph 2G)
O. ☐ Down Payment Verification (Paragraph 2H)
P. ☐ All Cash Verification (Paragraph 2L)
Q. ☐ Return of Statutory Disclosures (Paragraph 5A(2))
R. ☐ Return of Lead Disclosures (Paragraph 5A(2))
S. ☐ Receipt for Increased Deposit (Paragraph 16)
T. ☐ Escrow Evidence, Sale of Buyer's Property (C.A.R. Form COP, Paragraph A2 or A3)
U. ☐ _____
V. ☐ _____
W. ☐ _____

NOTE: Paragraph numbers refer to the California Residential Purchase Agreement (C.A.R. Form RPA-CA). Applicable paragraph numbers for each contingency or contractual action in other C.A.R. contracts are found in Contract Paragraph Matrix (C.A.R. Form CPM).

BUYER: If you do not remove the contingency(ies) (C.A.R. Forms RR and CR) or take the contractual actions specified above within 24 (or ☐) hours (but no less than the time specified in the Agreement) of receipt of this Notice to Buyer to Perform, Seller may cancel the Agreement.

_____ _____ _____ AM/PM
Seller **Date** **Time**

_____ _____ _____ AM/PM
Seller **Date** **Time**

(_____/_____) (Initials) **CONFIRMATION OF RECEIPT:** A Copy of this Signed Notice to Buyer to Perform was personally received by Buyer or authorized agent on _____ (date), at _____ AM/PM.

The copyright laws of the United States (TITLE 17 U.S. Code) forbid the unauthorized reproduction of this form by any means, including facsimile or computerized formats. Copyright © 2002-2009, CALIFORNIA ASSOCIATION OF REALTORS®
THIS FORM HAS BEEN APPROVED BY THE CALIFORNIA ASSOCIATION OF REALTORS® (C.A.R.) NO REPRESENTATION IS MADE AS TO THE LEGAL VALIDITY OR ADEQUACY OF ANY PROVISION IN ANY SPECIFIC TRANSACTION. A REAL ESTATE BROKER IS THE PERSON QUALIFIED TO ADVISE ON REAL ESTATE TRANSACTIONS. IF YOU DESIRE LEGAL OR TAX ADVICE, CONSULT AN APPROPRIATE PROFESSIONAL.
This form is available for use by the entire real estate industry. It is not intended to identify the user as a REALTOR®. REALTOR® is a registered collective membership mark which may be used only by members of the NATIONAL ASSOCIATION OF REALTORS® who subscribe to its Code of Ethics.

Published and Distributed by:
REAL ESTATE BUSINESS SERVICES, INC.
a subsidiary of the California Association of REALTORS®
525 South Virgil Avenue, Los Angeles, California 90020

NBP REVISED 04/09 (PAGE 1 OF 1) Print Date

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

SAMPLE

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/6 Residential Purchase and Sale Transactions/ §6.28A 6. Form: Short Sale Addendum (CAR Form SSA)

§6.28A 6. Form: Short Sale Addendum (CAR Form SSA)

Print

CALIFORNIA ASSOCIATION OF REALTORS ®

SHORT SALE ADDENDUM
(C.A.R. Form SSA, 4/09)

This is an addendum to the ☐ California Residential Purchase Agreement, ☐ Counter Offer, ☐ Other _____ _____ ("Agreement"), dated _____,
on property known as _____ ("Property"),
between _____ ("Buyer")
and _____ ("Seller").

A. SHORT SALE APPROVAL. This Agreement is contingent upon Seller's receipt of written consent from all existing secured lenders and lienholders ("Short-Sale Lenders"), no later than 5:00 P.M. on _____ (date) ("Short-Sale Contingency Date"), to reduce their respective loan balances by an amount sufficient to permit the proceeds from the sale of the Property to pay the existing balances on loans secured by the Property, real property taxes, brokerage commissions, closing costs, and other monetary obligations the Agreement requires Seller to pay at Close Of Escrow (including, but not limited to, escrow charges, title charges, documentary transfer taxes, prorations, retrofit costs and Repairs) without requiring Seller to place any funds into escrow or have any continuing obligation to Short-Sale Lender. If by the Short-Sale Contingency Date, either (i) Seller does not receive Short-Sale Lenders' written consent or (ii) Seller fails to give Buyer a copy of Short-Sale Lender's written consent then either Seller or Buyer, respectively, may cancel the Agreement in writing, and Buyer shall be entitled to a return of any deposit. Seller shall reasonably cooperate with existing Short-Sale lenders in the short-sale process.

B. TIME PERIODS: BUYER'S DEPOSIT CHECK:

1. Time periods in the Agreement for inspections, contingencies, covenants, and other obligations: **(i)** shall begin as specified in the Agreement; or **(ii)** (if checked) ☐ shall begin the Day After Seller delivers to Buyer written notice of Short-Sale Lenders' consent. However, even if Paragraph B1(ii) is checked, time periods for providing pre-approval/pre-qualification letters and verification of down payment and closing costs shall nonetheless begin as otherwise specified in the Agreement.
2. Buyer's deposit check shall be: **(i)** immediately handled as provided in the Agreement; or **(ii)** (if checked) ☐ held uncashed until the Day After Seller delivers to Buyer a written notice of Short Sale Lenders' consent.

C. NO ASSURANCE OF LENDER APPROVAL. Buyer and Seller understand that Short-Sale Lenders **(i)** are not obligated to give consent to a short-sale; **(ii)** may require Seller to forward any other offer received; and **(iii)** may give consent to other offers. Additionally, Short-Sale Lenders may require that, in order to obtain their approval for a short sale, some terms of the Agreement, such as the Close of Escrow, be amended or that Seller sign a personal note or some other obligation for all or a portion of the amount of the secured debt reduction. Buyer and Seller do not have to agree to any of Short-Sale Lenders' proposed terms. Buyer, Seller and Brokers do not have control over whether Short-Sale Lenders will consent to a short-sale, or any act, omission, or decision by any Short-Sale Lender in the short-sale process.

D. BUYER AND SELLER COSTS. Buyer and Seller acknowledge that each may incur costs in connection with rights or obligations under the Agreement. These costs may include, but are not limited to, payments for loan applications, inspections, appraisals, and other reports. Such costs will be the sole responsibility of the party incurring them, if Short-Sale Lenders do not consent to the transaction or either party cancels pursuant to the Agreement.

E. OTHER OFFERS. Unless otherwise agreed in writing, Seller may continue to market the Property despite acceptance of Buyer's offer, and to present to Short-Sale Lender(s) any additional offers that are received on the Property.

F. CREDIT, LEGAL AND TAX ADVICE. Seller is informed that a short-sale may have credit or legal consequences and may result in taxable income to Seller. **Seller is advised to seek advice from an attorney, certified public accountant or other expert regarding such potential consequences of a short-sale.**

By signing below, Buyer and Seller each acknowledge that they have read, understand, accept and have received a copy of this Short Sale Addendum.

Date _____ Date _____
Buyer _____ Seller _____
Buyer _____ Seller _____

The copyright laws of the United States (TITLE 17 U.S. Code) forbid the unauthorized reproduction of this form by any means, including facsimile or computerized formats. Copyright © 2007-2009, CALIFORNIA ASSOCIATION OF REALTORS®. ALL RIGHTS RESERVED.
THIS FORM HAS BEEN APPROVED BY THE CALIFORNIA ASSOCIATION OF REALTORS® (C.A.R.). NO REPRESENTATION IS MADE AS TO THE LEGAL VALIDITY OR ADEQUACY OF ANY PROVISION IN ANY SPECIFIC TRANSACTION. A REAL ESTATE BROKER IS THE PERSON QUALIFIED TO ADVISE ON REAL ESTATE TRANSACTIONS. IF YOU DESIRE LEGAL OR TAX ADVICE, CONSULT AN APPROPRIATE PROFESSIONAL.
This form is available for use by the entire real estate industry. It is not intended to identify the user as a REALTOR®. REALTOR® is a registered collective membership mark which may be used only by members of the NATIONAL ASSOCIATION OF REALTORS® who subscribe to its Code of Ethics.

Published and Distributed by:
REAL ESTATE BUSINESS SERVICES, INC.
a subsidiary of the California Association of REALTORS®
525 South Virgil Avenue, Los Angeles, California 90020

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

Comment: The forms in §§6.24-6.28A are reprinted with the permission of the California Association of Realtors®. Endorsement is not implied.

© The Regents of the University of California

§6.29 III. SELLER'S DISCLOSURES

A seller of residential real property in California has a duty to disclose to a buyer facts materially affecting the value or desirability of the property. The existence and contours of this duty are established in case law, and specific disclosure requirements are set forth in various federal and state statutes and local ordinances. The common law duty of disclosure is discussed in §§6.30-6.33. Statutory disclosure requirements are discussed in §§6.34-6.70.

© The Regents of the University of California

§6.30 A. Common Law Duty of Disclosure

There are no implied warranties in the sale of real property as to the quality or condition of the property, with the exception of new home construction. *Pollard v Saxe & Yolles Dev. Co*. (1974) 12 C3d 374, 115 CR 648; *East Hilton Drive Homeowners' Ass'n v Western Real Estate Exch., Inc.* (1982) 136 CA3d 630, 632, 186 CR 267; see also CC §1113 (specifying the covenants implied in a grant deed). Nevertheless, in all real estate transactions, whether commercial or residential, a common law duty of disclosure arises when the seller knows of facts materially affecting the value or desirability of the property that are known to or accessible only to the seller *and* knows that such facts are not known to, or within the reach of the diligent attention and observation of, the buyer. *Stevenson v Baum* (1998) 65 CA4th 159, 165, 75 CR2d 904; *Shapiro v Sutherland* (1998) 64 CA4th 1534, 1544, 76 CR2d 101. Whether a seller had actual knowledge of an undisclosed fact is a question of fact. 64 CA4th at 1544.

A seller does not have a duty to inspect property or investigate facts that may be material to a buyer. See *Corbett v Otts* (1962) 205 CA2d 78, 84, 22 CR 849; *Watt v Patterson* (1954) 125 CA2d 788, 792, 271 P2d 200. A seller who is ignorant of a fact will not be liable for failure to disclose it, no matter how material it may be. *San Diego Hospice v County of San Diego* (1995) 31 CA4th 1048, 1055, 37 CR2d 501. However, a seller will be deemed to have knowledge of facts actually known to the seller's current agents or employees or contained in the seller's records. *Herzog v Capital Co*. (1945) 27 C2d 349, 353, 164 P2d 8; *San Diego Hospice v County of San Diego, supra*. See also CC §2332 (agent's knowledge imputed to principal).

Breach of the duty of disclosure gives rise to a cause of action for both rescission and damages. *Shapiro,* 64 CA4th at 1544; *Karoutas v HomeFed Bank* (1991) 232 CA3d 767, 771, 283 CR 809. See also *Herzog v Capital Co., supra*; CC §1572 (actual fraud includes "suppression of that which is true by one having knowledge or belief of the fact"); CC §1710 (deceit includes suppression of a fact by one who is bound to disclose it). See also California Real Property Remedies and Damages, chaps 1, 3 (2d ed Cal CEB 2002).

© The Regents of the University of California

§6.31 1. Materiality

A fact must be disclosed if it is sufficiently material that it affects the property's value or desirability. *Shapiro v Sutherland* (1998) 64 CA4th 1534, 1544, 76 CR2d 101; *Lingsch v Savage* (1963) 213 CA2d 729, 737, 29 CR 201. Facts are deemed sufficiently material, in this context, if they would have a significant and measurable effect on the market value of the property. *Shapiro,* 64 CA4th at 1544; *Reed v King* (1983) 145 CA3d 261, 267, 193 CR 130; *Nece v Bennett* (1963) 212 CA2d 494, 496, 28 CR 117 (a fact that does not affect value of property is not material). Materiality may be decided on the basis of expert testimony or on the personal knowledge and experience of the trier of fact. *Alexander v McKnight* (1992) 7 CA4th 973, 977, 9 CR2d 453. Generally, whether information is sufficiently material to effect the value or desirability of property is a question of fact. *Calemine v Samuelson* (2009) 171 CA4th 153, 89 CR3d 495; *Stevenson v Baum* (1998) 65 CA4th 159, 165, 75 CR2d 904. In some cases, however, the issue may be resolved as a question of law. See *Reed,* 145 CA3d at 265, 267.

© The Regents of the University of California

§6.31A a. Physical Property Conditions

Case law has found certain physical conditions to be sufficiently material as to require disclosure. These include:

- Improvements constructed on fill (see, *e.g., Snelson v Ondulando Highlands Corp.* (1970) 5 CA3d 243, 251, 84 CR 800);
- Land subject to flooding (*Stowe v Nieto* (1945) 71 CA2d 375, 377, 162 P2d 837);
- Prior landslide (*Barnhouse v City of Pinole* (1982) 133 CA3d 171, 189, 183 CR 881);
- Structural defects, such as a roof leak (*Herzog v Capital Co.* (1945) 27 C2d 349, 352, 164 P2d 8);
- Termite infestation (*Godfrey v Steinpress* (1982) 128 CA3d 154, 177, 180 CR 95);
- Building code violations (*Lingsch,* 213 CA2d at 735; *Curran v Heslop* (1953) 115 CA2d 476, 480, 252 P2d 376);
- Improvements constructed without permit or in violation of zoning regulations (*Milmoe v Dixon* (1950) 101 CA2d 257, 261, 225 P2d 273; *Barder v McClung* (1949) 93 CA2d 692, 697, 209 P2d 808); and
- The existence of an easement (*Brady v Carman* (1960) 179 CA2d 63, 68, 3 CR 612).

© The Regents of the University of California

§6.31B b. Other Matters

Various matters unrelated to the physical condition of the property have been found to be sufficiently material as to require disclosure. These include:

- Noisy and disruptive neighbors (*Shapiro,* 64 CA4th at 1539 (neighbors, over a period of years, were the source of excessive noise and commotion, including loud arguments and late-night parties, causing seller to call the police on several occasions); *Alexander,* 7 CA4th at 977 (neighbors were an "overtly hostile family who delight[ed] in tormenting their neighbors" with noise and parties));
- Multiple murders at the property (*Reed,* 145 CA3d at 263);
- Use of the property violates the applicable zoning ordinance (*Coons v Gunn* (1968) 263 CA2d 594, 600, 69 CR 876); and
- The state is interested in buying and developing the property (*Storage Servs. v Oosterbaan* (1989) 214 CA3d 498, 508, 262 CR 689).

© The Regents of the University of California

§6.32 c. Corrected Conditions

A few cases have considered whether a seller has a duty to disclose to a buyer a property condition that has been repaired or corrected. In *Wood v Kalbaugh* (1974) 39 CA3d 926, 114 CR 673, for example, the court held that the seller's repair of a gas-line leak during the escrow period was not sufficiently material as to require disclosure. The leak had resulted from a rusted pipeline, was immediately replaced and tested by the seller, and later passed city safety requirements. 39 CA3d at 931. The *Wood* court was persuaded by the fact that the gas leak was readily repairable and had actually been repaired. 39 CA3d at 931. Similarly, in *Pagano v Krohn* (1997) 60 CA4th 1, 10, 70 CR2d 1, the court held that the past occurrence of moisture intrusion in the garage of the seller's condominium unit was not a material fact when the source of the moisture had been remedied well over a year before the sale by adjusting sprinklers so as not to spray the affected area and the buyer was otherwise aware of a general water intrusion problem affecting the entire condominium development.

The court reached a contrary conclusion in *Barnhouse v City of Pinole* (1982) 133 CA3d 171, 183 CR 881, holding that a seller's belief that preexisting slides, seeps, and springs had been permanently repaired did not excuse the failure to disclose them to the buyer. The court observed that when a seller has knowledge of "progressive destruction or substantial impairment," the seller has a duty to disclose the relevant circumstances even if he or she has reason to believe that the problem has been halted. 133 CA3d at 190. There was evidence in *Barnhouse* that the structural repair of the preexisting slides had been inadequate. 133 CA3d at 189.

PRACTICE TIP: These cases provide guidance for evaluating whether to disclose other types of past repairs. If the defect or condition can be repaired in a reliable fashion (*e.g.,* replacement of a rusted gas line) and has been so repaired, disclosure may not be necessary. But if the defect or condition is progressive in nature or likely to recur, and repair of the condition is therefore unreliable (*e.g.,* a landslide), the seller should disclose it. In questionable cases, or out of an abundance of caution, it is best to advise sellers to err on the side of disclosure.

© The Regents of the University of California

§6.32A 2. Scope and Extent of Disclosure

Once a seller discloses "essential facts" about a material condition, it has satisfied its duty of disclosure and need not "elaborate" on those facts. *Calemine v Samuelson* (2009) 171 CA4th 153, 161, 89 CR3d 495; *Pagano v Krohn* (1997) 60 CA4th 1, 10, 70 CR2d 1. See also *Sweat v Hollister* (1995) 37 CA4th 603, 609, 43 CR2d 399, disapproved on other grounds in *Santisas v Goodin* (1998) 17 C4th 599, 71 CR2d 830 (seller does not have duty to advise or opine on legal ramifications of disclosed fact); *Stevenson v Baum* (1998) 65 CA4th 159, 166, 75 CR2d 904 (notice in purchase contract that title is subject to easements of record satisfied seller's disclosure duty when recorded easement agreement revealed essential facts about easement).

In *Calemine v Samuelson, supra,* plaintiff-buyers sued the seller of a condominium for failing to fully disclose the history of water intrusion in the development and related construction litigation. The seller had made written and oral disclosures to the buyer regarding the existence of past water intrusion, outlined repairs that had been made, and urged the buyers in writing to obtain a physical inspection. Evidence of the past water intrusion was confirmed during the professional property inspection. A few years later, the buyers experienced water intrusion in their unit and learned that, 20 years earlier, the HOA and individual unit owners had filed construction defect lawsuits against the developer and subcontractor while the seller was on the HOA board. The buyers also learned that the HOA settled for a fraction of their consultant's estimated repair costs and then performed only a partial repair. None of these facts were disclosed to the buyers.

The court rejected the buyers' contention that the seller was required to disclose more detail about the type and scope of repairs. The court found such further information to be an "elaboration" on the basic disclosed fact, which is not part of the seller's duty of disclosure. 171 CA4th at 164. Nevertheless, the appellate court reversed the trial court, finding that a triable issue of fact remained as to whether the prior lawsuits were material facts that the seller should have disclosed.

The court held that a seller's common law duty of disclosure encompasses disclosure of a lawsuit affecting property but not the details of the lawsuit. 171 CA4th at 166. The court observed that disclosure of the lawsuits would have permitted the buyer to examine the details of those actions and evaluate its purchase in light of that information. Without the predicate disclosure of the existence of the lawsuits, these facts were not within the buyer's diligent attention and thus had to be disclosed by the seller. 171 CA4th at 166. See also *Assilzadeh v California Fed. Bank* (2000) 82 CA4th 399, 98 CR2d 176; *Pagano,* 60 CA4th at 10 (once buyer is made aware that water intrusion resulted in litigation against developer, details about lawsuit were within buyer's diligent attention and need not be disclosed by seller).

PRACTICE TIP: Determining what constitutes an "essential fact" as opposed to an "elaboration" will depend on the facts and circumstances of each particular case and requires the exercise of sound judgment. Although *Calemine* does not hold that past litigation is always material and must be disclosed in every case, it comes close to doing so. It is advisable to disclose all past litigation which relates to a disclosed material condition, particularly conditions such as water intrusion that often are not reliably repaired or otherwise may recur. This effectively shifts the burden to the buyer to investigate and discover details that may include material facts. It is also advisable for a buyer, on receipt of a litigation disclosure from a seller, to fully investigate the allegations and ultimate disposition of the lawsuit. In addition to reviewing public records, a buyer can request specific information from the seller, which may effectively shift the burden back to the seller to "elaborate" on the original disclosure.

© The Regents of the University of California

§6.33 3. Public Policy Limitations on the Duty to Disclose

The legislature has limited the duty of disclosure in certain situations when it has concluded that public policy concerns outweigh the benefits of private disclosure. For example, there is a strong public policy in California favoring the establishment of various types of residential care facilities and day care homes to provide a wide range of nonmedical care and social services. See the California Community Care Facilities Act (Health & S C §§1500-1567.8). In furtherance of that policy, the Act provides that, in connection with the transfer of real property, a licensed care facility that serves six or fewer persons is to be considered a residential use of property by a single family. Health & S C §1566.5. The fact that a single family lives at a property is not material and therefore need not be disclosed. Moreover, although no court has addressed the issue, the California Attorney General has consistently opined that care facilities serving six or fewer persons are not nuisances because they have been expressly authorized by statute (CC §3482), and their existence in a neighborhood is not a material fact that must be disclosed. 79 Ops Cal Atty Gen 112 (1996) (domestic violence shelter is not a nuisance and need not be disclosed by a seller of residential property). However, in response to a direct inquiry, disclosure is permitted as long as it is factual and not used to aid discrimination against or segregation of the facility within the community. See 73 Ops Cal Atty Gen 58, 67 (1990).

PRACTICE TIP: As no court has yet addressed this disclosure issue, it may be advisable for a seller to disclose the existence of a licensed care facility serving *more than* six persons, particularly if it is close to the property. The disclosure should be strictly factual and avoid statements that might be construed as discriminatory.

© The Regents of the University of California

§6.34 B. Statutory Disclosure Requirements

Numerous federal and state statutes and local ordinances require sellers to make specific disclosures to buyers of residential real property. These laws reflect legislative determinations that certain matters are always sufficiently material such that their disclosure should be mandated. See, *e.g., Realmuto v Gagnard* (2003) 110 CA4th 193, 200, 1 CR3d 569 (identifying California legislature's stated purposes in enacting statutory transfer disclosure requirements). These statutory disclosure requirements do not replace the common law duty to disclose facts that materially affect the value or desirability of a property. See CC §§1102.1, 1102.8.

Documentation of residential transactions in California often includes a jumble of disjointed standard form disclosures that are required to discharge various statutory obligations. The extent to which a real estate licensee in a given transaction explains, or is qualified to explain, these standard forms will vary depending on the skill and experience of the licensee. Attorneys can assist both buyers and sellers by explaining the legal significance of the underlying statutory obligations and making sure that all required statutory disclosures have been made.

Federal and state (and a few local) disclosure requirements that apply to the typical residential sale transaction are discussed in §§6.35-6.70. These requirements are organized according to the authorizing statutory scheme or substantively as follows:

- Transfer disclosures (§§6.35-6.46A);
- Local disclosures (§§6.38-6.41);
- Natural hazards disclosures (§§6.47-6.50);
- Health and safety disclosures (§§6.51-6.59);
- Common interest development (CID) disclosures (§§6.60-6.63);
- New home sales disclosures (§6.64); and
- Miscellaneous disclosures (§§6.65-6.70).

© The Regents of the University of California

§6.35 1. Transfer Disclosures

Civil Code §§1102-1102.17 set forth various disclosures that must be made in every transfer of real property or a residential stock cooperative improved with one to four dwelling units, by sale, exchange, installment land sale contract (as defined in CC §2985), lease with an option to purchase, any other option to purchase, or ground lease coupled with improvements. CC §1102(a). These disclosures must also be made in the resale of a manufactured home or a mobilehome that is classified as personal property and intended for use as a residence. CC §1102(b). See Health & S C §§18007, 18008 for the definitions of manufactured homes and mobilehomes. The individual required disclosures are discussed separately in §§6.36-6.46.

Civil Code §§1102-1102.17 do not apply to the following transactions, which are exempt:

- Transfers that require a subdivision public report under Bus & P C §11018.1 or that can be made without a public report under Bus & P C §11010.4 (CC §1102.2(a));
- Transfers under court order (*e.g.,* probate sales, foreclosure sales, transfers by a bankruptcy trustee, transfers under to a writ of execution) (CC §1102.2(b));
- Transfers by foreclosure sale after default or by deed in lieu of foreclosure; transfers by a mortgagee or beneficiary under a deed of trust who acquired the property at a trustee's sale, foreclosure sale, or by deed in lieu of foreclosure; or transfers by foreclosure of a security interest in a manufactured home or mobilehome; see *Assilzadeh v California Fed. Bank* (2000) 82 CA4th 399, 98 CR2d 176 (CC §1102.2(c));
- Transfers by a fiduciary in the course of administering a decedent's estate, guardianship, conservatorship, or trust; however, this exemption does not apply to a transfer when the trustee is a natural person who is the sole trustee of a revocable trust and is the former owner of the property or an occupant of the property within the preceding year (CC §1102.2(d));
- Transfers between co-owners (CC §1102.2(e));
- Transfers to a spouse or persons "in the lineal line of consanguinity" (direct ancestors or descendants) (CC §1102.2(f));
- Transfers between spouses in connection with marital dissolution proceedings (CC §1102.2(g));
- Transfers by the State Controller in administering the Unclaimed Property Law (CCP §§1500-1582) (CC §1102.2(h));
- Transfers resulting from failure to pay property taxes under Rev & T C §3771 (CC §1102.2(i)); and
- Transfers or exchanges to or from any governmental entity (CC §1102.2(j)).

Even in exempt transactions, however, the transferor still has a common law duty of disclosure. *Karoutas v HomeFed Bank* (1991) 232 CA3d 767, 773, 283 CR 809. For a discussion of common law standards, see §§6.30-6.33.

When CC §§1102-1102.17 apply, any waiver of the requirements they set forth is void as against public policy. CC §1102(c). See CC §1102.1(a) ("as is" clause does not waive duty to deliver transfer disclosure statement required by §1102.6). The transfer disclosures must be made in good faith, for which the standard is honesty in fact in the conduct of the transaction. CC §1102.7. Delivery of transfer disclosures must be by personal delivery or mail to the transferee or prospective transferee or his or her spouse, unless otherwise provided in the purchase contract. CC §1102.10. The real estate licensees in the transaction are responsible for delivering the transfer disclosures. CC §1101.12. An escrow agent is not an agent of the transferor or transferee for purposes of fulfilling disclosure requirements, unless otherwise agreed in writing. CC §1101.11.

If any of the transfer disclosures are made after execution of a purchase contract, the buyer or other transferee has 3 days after delivery in person, or 5 days after delivery by deposit in the mail, to terminate his or her offer by delivery of written notice to the transferor or the transferor's agent. CC §1102.3(b). See *Realmuto v Gagnard* (2003) 110 CA4th 193, 201, 1 CR3d 569 (when buyer's offer was accepted before transfer disclosures were delivered, the right to "terminate an offer" in §1102.3 is, in fact, a right to rescind a contract). A previously delivered transfer disclosure may be amended in writing by the seller or his or her agent, but such amendment triggers the transferee's termination right. CC §1102.9.

PRACTICE TIP: Delivery of transfer disclosures to the transferee's agent may not be sufficient to trigger the applicable 3- or 5-day rescission right. Thus, in every transaction in which transfer disclosures are delivered after the purchase contract has been executed, the transferor (or agent) should make sure that the transferee has actually received each transfer disclosure, signed and dated it, and acknowledged receipt, to establish the date from

which the rescission right runs for that disclosure. Better yet, the safest course is to deliver transfer disclosures to a prospective buyer before accepting a purchase offer and to require the buyer to submit a signed and dated acknowledgement of receipt with the offer. The transferor should be careful to complete the transfer disclosures fully and accurately to avoid the need for an amendment that would retrigger the rescission period.

Neither the transferor nor the agents in the transaction will be liable for an error, inaccuracy, or omission in any transfer disclosure if the information disclosed was not within their personal knowledge, was based on information provided by public agencies or certain qualified professionals, and ordinary care was exercised in obtaining and transmitting such information. CC §1102.4(a). For purposes of this liability protection, qualified professionals include a licensed engineer, land surveyor, geologist, structural pest control operator, contractor, or other expert when dealing with matters within the scope of the individual's professional license or expertise. CC §1102.4(c). Delivery of information by such qualified professionals relieves the transferor and agents of any further duty of disclosure with respect to that item (assuming such persons do not have actual knowledge of material facts pertaining to that item). CC §1102.4(b).

PRACTICE TIP: It is now common for California sellers to have third party qualified professionals complete "substitute disclosures" to fulfill the transfer disclosure requirements, except for the disclosures required on the Transfer Disclosure Statement (see §6.36), which must be completed by the transferor and agents. Two commonly used substitute disclosure companies are JCP Geologists and Property ID. See the Directory for their website addresses. The cost for a report covering the substitute transfer disclosures is generally less than $100, and the providers expressly indemnify the transferor for liability resulting from errors, inaccuracy, or omissions in the substitute disclosures. Additional disclosures are also available from both providers.

If information required to be disclosed is unknown or unavailable to the transferor and a reasonable effort is made to obtain such information, the transferor may use an approximation, provided he or she identifies it as such and it is reasonable and based on the best information available and not made to evade disclosure requirements. CC §1102.5. If a transfer disclosure is rendered inaccurate because of events that occur after its delivery, the resulting inaccuracy does not violate the transfer disclosure requirements. CC §1102.5. If, however, such subsequent events are actually known to the transferor or agent and are material, they must be disclosed under the common law duty. See §§6.30-6.33.

A failure to comply with the requirements of CC §§1102-1102.17 does not, by itself, invalidate a transfer. However, a person who willfully or negligently fails to discharge the transfer disclosure duties will be liable for actual damages suffered by the transferee. CC §1102.13. See *Saunders v Taylor* (1996) 42 CA4th 1538, 1543, 50 CR2d 395 ("actual damages" as used in CC §1102.13 means "out-of-pocket" damages as measured by CC §3343).

© The Regents of the University of California

§6.36 a. Real Estate Transfer Disclosure Statement

The heart of the transfer disclosures is the Real Estate Transfer Disclosure Statement (TDS). The TDS is a standard form set forth in CC §1102.6, on which the transferor and agents must make certain transfer disclosures. The California Association of Realtors'® (CAR) Form TDS, which reproduces the statutory form, is commonly used. See §6.37. The legislature has also prescribed a statutory form to be used to make the disclosures required by CC §1102(b) in the case of the resale of a manufactured home or mobilehome that is classified as personal property. See CC §1102.6d. The TDS is not a warranty or a part of the purchase contract. *Brasier v Sparks* (1993) 17 CA4th 1756, 1760, 22 CR2d 1.

When required, the TDS must be delivered as soon as practicable before either (1) transfer of title, in the case of a sale, or (2) execution of a contract if the transaction involves one of the other forms of transfer covered. CC §1102.3. The transferor must indicate compliance with transfer disclosure requirements either on the purchase contract, lease, or an addendum thereto, or in a separate document. CC §1102.3(b). If the seller fails to deliver a TDS to the buyer, the seller cannot later pursue an action for specific performance or breach of contract against the buyer, because delivery of the TDS is a nonwaivable condition precedent to the buyer's duty to perform. *Realmuto v Gagnard* (2003) 110 CA4th 193, 201, 1 CR3d 569.

The TDS form has four parts to be completed. See §6.37. Part I, Coordination With Other Disclosure Forms, requires the seller to specify which substitute transfer disclosures the seller is delivering to the buyer and states that the substitute disclosures are intended to satisfy disclosure obligations on the TDS when the subject matter is the same. Parts III and IV, respectively, are to be completed by the listing agent and the selling (buyer's) agent, if any, to disclose material facts discovered during the agent's reasonably competent and diligent visual inspection of accessible areas of property as required by CC §2079.

Part II, Seller's Information, is to be completed by the seller. It has three subparts. Subpart A lists various components of a residential property and requires the seller to check off the items that apply to the subject property. After doing so, the seller must state, to the best of seller's knowledge, whether any of the components identified "are not in operating condition." For those that are not operable, the seller is required to describe the condition. Subpart B requires the seller to disclose whether he or she is aware of "any significant defects/malfunctions" in any structural component of the property. If so, the seller is required to explain. Subpart C requires the seller to state whether he or she is aware of any of 16 problems that may affect the property and, if so, to explain. These problems include many of the items that have been deemed sufficiently material as to require disclosure under the common law standard. They include various environmental hazards, adjacent-neighbor issues (*e.g.,* common fences or walls, encroachments, easements), common interest development disclosures, nuisances, governmental notices or litigation affecting the property, zoning or permit noncompliance or violations, and physical conditions (*e.g.,* fill, settling, flooding, drainage problems, major damage from natural hazards).

PRACTICE TIP: The seller must exercise a great deal of judgment in completing the TDS. Although Subparts A and B only require disclosure of components that are "not in operating condition" or have "*significant* defects/malfunctions," to avoid future disputes it is generally advisable for a seller to disclose all known operational difficulties and any other known property defects or malfunctions.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/6 Residential Purchase and Sale Transactions/ §6.37 b. Form: Real Estate Transfer Disclosure Statement (CC §1102.6)

§6.37 b. Form: Real Estate Transfer Disclosure Statement (CC §1102.6)

Print

CALIFORNIA ASSOCIATION OF REALTORS®

REAL ESTATE TRANSFER DISCLOSURE STATEMENT

(CALIFORNIA CIVIL CODE §1102, ET SEQ.)

(C.A.R. Form TDS, Revised 10/03)

THIS DISCLOSURE STATEMENT CONCERNS THE REAL PROPERTY SITUATED IN THE CITY OF _____, COUNTY OF _____, STATE OF CALIFORNIA, DESCRIBED AS _____.

THIS STATEMENT IS A DISCLOSURE OF THE CONDITION OF THE ABOVE DESCRIBED PROPERTY IN COMPLIANCE WITH SECTION 1102 OF THE CIVIL CODE AS OF (date) _____. IT IS NOT A WARRANTY OF ANY KIND BY THE SELLER(S) OR ANY AGENT(S) REPRESENTING ANY PRINCIPAL(S) IN THIS TRANSACTION, AND IS NOT A SUBSTITUTE FOR ANY INSPECTIONS OR WARRANTIES THE PRINCIPAL(S) MAY WISH TO OBTAIN.

I. COORDINATION WITH OTHER DISCLOSURE FORMS

This Real Estate Transfer Disclosure Statement is made pursuant to Section 1102 of the Civil Code. Other statutes require disclosures, depending upon the details of the particular real estate transaction (for example: special study zone and purchase-money liens on residential property).

Substituted Disclosures: The following disclosures and other disclosures required by law, including the Natural Hazard Disclosure Report/Statement that may include airport annoyances, earthquake, fire, flood, or special assessment information, have or will be made in connection with this real estate transfer, and are intended to satisfy the disclosure obligations on this form, where the subject matter is the same:

☐ Inspection reports completed pursuant to the contract of sale or receipt for deposit.
☐ Additional inspection reports or disclosures: _____

_____

II. SELLER'S INFORMATION

The Seller discloses the following information with the knowledge that even though this is not a warranty, prospective Buyers may rely on this information in deciding whether and on what terms to purchase the subject property. Seller hereby authorizes any agent(s) representing any principal(s) in this transaction to provide a copy of this statement to any person or entity in connection with any actual or anticipated sale of the property.

THE FOLLOWING ARE REPRESENTATIONS MADE BY THE SELLER(S) AND ARE NOT THE REPRESENTATIONS OF THE AGENT(S), IF ANY. THIS INFORMATION IS A DISCLOSURE AND IS NOT INTENDED TO BE PART OF ANY CONTRACT BETWEEN THE BUYER AND SELLER.

Seller ☐ is ☐ is not occupying the property.

A. The subject property has the items checked below (read across):

☐ Range	☐ Oven	☐ Microwave
☐ Dishwasher	☐ Trash Compactor	☐ Garbage Disposal
☐ Washer/Dryer Hookups		☐ Rain Gutters
☐ Burglar Alarms	☐ Smoke Detector(s)	☐ Fire Alarm
☐ TV Antenna	☐ Satellite Dish	☐ Intercom
☐ Central Heating	☐ Central Air Conditioning	☐ Evaporator Cooler(s)
☐ Wall/Window Air Conditioning	☐ Sprinklers	☐ Public Sewer System
☐ Septic Tank	☐ Sump Pump	☐ Water Softener
☐ Patio/Decking	☐ Built-in Barbecue	☐ Gazebo
☐ Sauna		
☐ Hot Tub	☐ Pool	☐ Spa
☐ Locking Safety Cover*	☐ Child Resistant Barrier*	☐ Locking Safety Cover*
☐ Security Gate(s)	☐ Automatic Garage Door Opener(s)*	☐ Number Remote Controls ____
Garage: ☐ Attached	☐ Not Attached	☐ Carport
Pool/Spa Heater: ☐ Gas	☐ Solar	☐ Electric
Water Heater: ☐ Gas	☐ Water Heater Anchored, Braced, or Strapped*	
Water Supply: ☐ City	☐ Well	☐ Private Utility or
Gas Supply: ☐ Utility	☐ Bottled	Other _____
☐ Window Screens	☐ Window Security Bars ☐ Quick Release Mechanism on Bedroom Windows*	

Exhaust Fan(s) in _____ 220 Volt Wiring in _____ Fireplace(s) in _____
☐ Gas Starter _____ ☐ Roof(s): Type: _____ Age: _____ (approx.)
☐ Other: _____

Are there, to the best of your (Seller's) knowledge, any of the above that are not in operating condition? ☐ Yes ☐ No. If yes, then describe. (Attach additional sheets if necessary): _____

_____

(*see footnote on page 2)

The copyright laws of the United States (Title 17 U.S. Code) forbid the unauthorized reproduction of this form, or any portion thereof, by photocopy machine or any other means, including facsimile or computerized formats. Copyright © 1991-2003, CALIFORNIA ASSOCIATION OF REALTORS®, INC. ALL RIGHTS RESERVED.

Buyer's Initials (_____)(_____)
Seller's Initials (_____)(_____)

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

Print

Property Address: _____ Date: _____

B. Are you (Seller) aware of any significant defects/malfunctions in any of the following? ☐ Yes ☐ No. If yes, check appropriate space(s) below.

☐ Interior Walls ☐ Ceilings ☐ Floors ☐ Exterior Walls ☐ Insulation ☐ Roof(s) ☐ Windows ☐ Doors ☐ Foundation ☐ Slab(s)
☐ Driveways ☐ Sidewalks ☐ Walls/Fences ☐ Electrical Systems ☐ Plumbing/Sewers/Septics ☐ Other Structural Components

(Describe: _____
_____
_____
_____)

If any of the above is checked, explain. (Attach additional sheets if necessary.): _____
_____
_____
_____
_____

*This garage door opener or child resistant pool barrier may not be in compliance with the safety standards relating to automatic reversing devices as set forth in Chapter 12.5 (commencing with Section 19890) of Part 3 of Division 13 of, or with the pool safety standards of Article 2.5 (commencing with Section 115920) of Chapter 5 of Part 10 of Division 104 of, the Health and Safety Code. The water heater may not be anchored, braced, or strapped in accordance with Section 19211 of the Health and Safety Code. Window security bars may not have quick release mechanisms in compliance with the 1995 edition of the California Building Standards Code.

C. Are you (Seller) aware of any of the following:

1. Substances, materials, or products which may be an environmental hazard such as, but not limited to, asbestos, formaldehyde, radon gas, lead-based paint, mold, fuel or chemical storage tanks, and contaminated soil or water on the subject property ..... ☐ Yes ☐ No
2. Features of the property shared in common with adjoining landowners, such as walls, fences, and driveways, whose use or responsibility for maintenance may have an effect on the subject property ..... ☐ Yes ☐ No
3. Any encroachments, easements or similar matters that may affect your interest in the subject property ..... ☐ Yes ☐ No
4. Room additions, structural modifications, or other alterations or repairs made without necessary permits ..... ☐ Yes ☐ No
5. Room additions, structural modifications, or other alterations or repairs not in compliance with building codes .... ☐ Yes ☐ No
6. Fill (compacted or otherwise) on the property or any portion thereof ..... ☐ Yes ☐ No
7. Any settling from any cause, or slippage, sliding, or other soil problems ..... ☐ Yes ☐ No
8. Flooding, drainage or grading problems ..... ☐ Yes ☐ No
9. Major damage to the property or any of the structures from fire, earthquake, floods, or landslides ..... ☐ Yes ☐ No
10. Any zoning violations, nonconforming uses, violations of "setback" requirements ..... ☐ Yes ☐ No
11. Neighborhood noise problems or other nuisances ..... ☐ Yes ☐ No
12. CC&R's or other deed restrictions or obligations ..... ☐ Yes ☐ No
13. Homeowners' Association which has any authority over the subject property ..... ☐ Yes ☐ No
14. Any "common area" (facilities such as pools, tennis courts, walkways, or other areas co-owned in undivided interest with others) ..... ☐ Yes ☐ No
15. Any notices of abatement or citations against the property ..... ☐ Yes ☐ No
16. Any lawsuits by or against the Seller threatening to or affecting this real property, including any lawsuits alleging a defect or deficiency in this real property or "common areas" (facilities such as pools, tennis courts, walkways, or other areas co-owned in undivided interest with others) ..... ☐ Yes ☐ No

If the answer to any of these is yes, explain. (Attach additional sheets if necessary.): _____
_____
_____
_____
_____

Seller certifies that the information herein is true and correct to the best of the Seller's knowledge as of the date signed by the Seller.

Seller_____ Date _____

Seller_____ Date _____

Buyer's Initials (_____)(_____)
Seller's Initials (_____)(_____)

Reviewed by _____ Date _____

Copyright © 1991-2003, CALIFORNIA ASSOCIATION OF REALTORS®, INC.

EQUAL HOUSING OPPORTUNITY

REAL ESTATE TRANSFER DISCLOSURE STATEMENT (TDS PAGE 2 OF 3)

Print

SAMPLE

Property Address: _____ Date: _____

III. AGENT'S INSPECTION DISCLOSURE

(To be completed only if the Seller is represented by an agent in this transaction.)

THE UNDERSIGNED, BASED ON THE ABOVE INQUIRY OF THE SELLER(S) AS TO THE CONDITION OF THE PROPERTY AND BASED ON A REASONABLY COMPETENT AND DILIGENT VISUAL INSPECTION OF THE ACCESSIBLE AREAS OF THE PROPERTY IN CONJUNCTION WITH THAT INQUIRY, STATES THE FOLLOWING:

☐ Agent notes no items for disclosure.

☐ Agent notes the following items: _____

_____

_____

_____

_____

Agent (Broker Representing Seller) _____ By _____ Date _____
(Please Print) (Associate Licensee or Broker Signature)

IV. AGENT'S INSPECTION DISCLOSURE

(To be completed only if the agent who has obtained the offer is other than the agent above.)

THE UNDERSIGNED, BASED ON A REASONABLY COMPETENT AND DILIGENT VISUAL INSPECTION OF THE ACCESSIBLE AREAS OF THE PROPERTY, STATES THE FOLLOWING:

☐ Agent notes no items for disclosure.

☐ Agent notes the following items: _____

_____

_____

_____

_____

Agent (Broker Obtaining the Offer) _____ By _____ Date _____
(Please Print) (Associate Licensee or Broker Signature)

V. BUYER(S) AND SELLER(S) MAY WISH TO OBTAIN PROFESSIONAL ADVICE AND/OR INSPECTIONS OF THE PROPERTY AND TO PROVIDE FOR APPROPRIATE PROVISIONS IN A CONTRACT BETWEEN BUYER AND SELLER(S) WITH RESPECT TO ANY ADVICE/INSPECTIONS/DEFECTS.

I/WE ACKNOWLEDGE RECEIPT OF A COPY OF THIS STATEMENT.

Seller _____ Date _____ Buyer _____ Date _____

Seller _____ Date _____ Buyer _____ Date _____

Agent (Broker Representing Seller) _____ By _____ Date _____
(Please Print) (Associate Licensee or Broker Signature)

Agent (Broker Obtaining the Offer) _____ By _____ Date _____
(Please Print) (Associate Licensee or Broker Signature)

SECTION 1102.3 OF THE CIVIL CODE PROVIDES A BUYER WITH THE RIGHT TO RESCIND A PURCHASE CONTRACT FOR AT LEAST THREE DAYS AFTER THE DELIVERY OF THIS DISCLOSURE IF DELIVERY OCCURS AFTER THE SIGNING OF AN OFFER TO PURCHASE. IF YOU WISH TO RESCIND THE CONTRACT, YOU MUST ACT WITHIN THE PRESCRIBED PERIOD.

A REAL ESTATE BROKER IS QUALIFIED TO ADVISE ON REAL ESTATE. IF YOU DESIRE LEGAL ADVICE, CONSULT YOUR ATTORNEY.

THIS FORM HAS BEEN APPROVED BY THE CALIFORNIA ASSOCIATION OF REALTORS® (C.A.R.). NO REPRESENTATION IS MADE AS TO THE LEGAL VALIDITY OR ADEQUACY OF ANY PROVISION IN ANY SPECIFIC TRANSACTION. A REAL ESTATE BROKER IS THE PERSON QUALIFIED TO ADVISE ON REAL ESTATE TRANSACTIONS. IF YOU DESIRE LEGAL OR TAX ADVICE, CONSULT AN APPROPRIATE PROFESSIONAL.
This form is available for use by the entire real estate industry. It is not intended to identify the user as a REALTOR®. REALTOR® is a registered collective membership mark which may be used only by members of the NATIONAL ASSOCIATION OF REALTORS® who subscribe to its Code of Ethics.

SURE TRAC The System for Success®
Published and Distributed by:
REAL ESTATE BUSINESS SERVICES, INC.
a subsidiary of the California Association of REALTORS®
525 South Virgil Avenue, Los Angeles, California 90020

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

© The Regents of the University of California

SAMPLE

c. Local Disclosure and Transfer Requirements

§6.38 (1) Local Option Transfer Disclosure Statement

In addition to the disclosures on the TDS, CC §1102.6a(a) authorizes a city or county to require disclosures on the Local Option Real Estate Transfer Disclosure Statement set forth in §1102.6(b). See §6.39. A city or county may use a different disclosure form in connection with ordinances adopted before July 1, 1990, and may specify addenda to the Local Option TDS to facilitate the required disclosure. CC §1102.6a(a), (c).

PRACTICE TIP: Counsel should investigate whether the city or county in which the property is located has adopted a Local Option TDS or mandated other local disclosures or transfer requirements. A real estate licensee who routinely sells property within that city and county can facilitate compliance with such local requirements.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/6 Residential Purchase and Sale Transactions/ §6.39 (2) Form: Local Transfer Disclosure Statement (CC §1102.6a)

§6.39 (2) Form: Local Transfer Disclosure Statement (CC §1102.6a)

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

LOCAL OPTION

REAL ESTATE TRANSFER DISCLOSURE STATEMENT

THIS DISCLOSURE STATEMENT CONCERNS THE REAL PROPERTY SITUATED IN THE CITY OF _____, COUNTY OF _____, STATE OF CALIFORNIA, DESCRIBED AS _____. THIS STATEMENT IS A DISCLOSURE OF THE CONDITION OF THE ABOVE DESCRIBED PROPERTY IN COMPLIANCE WITH ORDINANCE NO. _____ OF THE _____ CITY OR COUNTY CODE AS OF _____, 20_ _. IT IS NOT A WARRANTY OF ANY KIND BY THE SELLER(S) OR ANY AGENT(S) REPRESENTING ANY PRINCIPAL(S) IN THIS TRANSACTION, AND IS NOT A SUBSTITUTE FOR ANY INSPECTIONS OR WARRANTIES THE PRINCIPAL(S) MAY WISH TO OBTAIN.

I

SELLER'S INFORMATION

The Seller discloses the following information with the knowledge that even though this is not a warranty, prospective Buyers may rely on this information in deciding whether and on what terms to purchase the subject property. Seller hereby authorizes any agent(s) representing any principal(s) in this transaction to provide a copy of this statement to any person or entity in connection with any actual or anticipated sale of the property.

THE FOLLOWING ARE REPRESENTATIONS MADE BY THE SELLER(S) AS REQUIRED BY THE CITY OR COUNTY OF _____, AND ARE NOT THE REPRESENTATIONS OF THE AGENT(S), IF ANY. THIS INFORMATION IS A DISCLOSURE AND IS NOT INTENDED TO BE PART OF ANY CONTRACT BETWEEN THE BUYER AND SELLER.

1._____

_____

2._____

_____

(Example: Adjacent land is zoned for timber production which may be subject to harvest.)

_____

Seller certifies that the information herein is true and correct to the best of the Seller's knowledge as of the date signed by the Seller.

Seller _____ Date _____

Seller _____ Date _____

II

BUYER(S) AND SELLER(S) MAY WISH TO OBTAIN PROFESSIONAL ADVICE AND/OR INSPECTIONS OF THE PROPERTY AND TO PROVIDE FOR APPROPRIATE PROVISIONS IN A CONTRACT BETWEEN BUYER AND SELLER(S) WITH RESPECT TO ANY ADVICE/INSPECTIONS/DEFECTS.

I/WE ACKNOWLEDGE RECEIPT OF A COPY OF THIS STATEMENT.

Seller _____ Date _____ Buyer _____ Date _____

Seller _____ Date _____	**Buyer _____ Date _____**
Agent (Broker Representing Seller) _____	**By _____ Date _____ (Associate Licensee or Broker-Signature)**
Agent (Broker Obtaining Offer) _____	**By _____ Date _____ (Associate Licensee or Broker-Signature)**

A REAL ESTATE BROKER IS QUALIFIED TO ADVISE ON REAL ESTATE. IF YOU DESIRE LEGAL ADVICE, CONSULT YOUR ATTORNEY.

© The Regents of the University of California

§6.40 (3) Residential Building Records Report

Cities may, by ordinance, require the owner of residential property to obtain from the city a report of residential building records (3-R Report) showing the authorized use, occupancy, and zoning classifications of the property. Govt C §38780. The ordinance must provide that it is unlawful for the owner to sell or exchange residential real property without having obtained and delivered a 3-R Report to the transferee. Govt C §38783. When required, the owner must deliver the 3-R Report to the buyer or other transferee prior to "the consummation of the sale or exchange." Govt C §38781. Failure to deliver a 3-R Report, when required, does not invalidate the sale or exchange unless the act or omission would be a valid ground for rescission independent of the statutory requirement. Govt C §38785. These requirements do not apply to the first sale of residential property in a subdivision if a final map has been duly approved and recorded within 2 years before the first sale. Govt C §38784.

© The Regents of the University of California

§6.41 (4) "Point of Sale" Ordinances

Many localities, particularly in urban areas of the state, have enacted ordinances mandating compliance with certain governmental retrofit standards or requiring certain inspections and reports to be completed before the close of escrow. These ordinances vary depending on local conditions and concerns.

EXAMPLE: The City of Berkeley has enacted a comprehensive Residential Energy Conservation Ordinance (RECO). See Berkeley Muni C ch 19.16. RECO provides that, before the sale or exchange of any residential structure or unit, the seller or agent (if any) must provide the buyer with a copy of a certificate of compliance with the ordinance. Berkeley Muni C ch 19.16.070.

© The Regents of the University of California

§6.42 d. Mello-Roos Act and 1915 Bond Act

If the seller's property is subject to a continuing lien securing the levy of special taxes under the Mello-Roos Community Facilities Act of 1982 (Govt C §§53311-53368.3) or a fixed lien assessment collected in installments to secure bonds issued under the Improvement Bond Act of 1915 (Str & H C §§8500-8887), the seller must make a good faith effort to obtain a disclosure notice regarding the special tax or assessment, as provided for in Govt C §§53340.2 and 53754, from each local agency that levies such a special tax or collects such assessment installments, and deliver the notice or notices to the prospective buyer. CC §1102.6b(b). These taxes and assessments, when they apply, can materially increase the cost of property ownership. Transfers that do not require a TDS are also exempt from this notice requirement. CC §1102.6b(a)(1). See CC §1102.2 for exempt transfers (listed in §6.35). A seller may obtain the required notices directly from the agencies involved or, as is more common, contract with a nongovernmental source to provide the disclosure notice. CC §1102.6b(d). Once a seller delivers the required special tax or assessment notices, the seller need not provide any additional information and is deemed to have satisfied his or her responsibility to inform the buyer on the subject. CC §1102.6(e).

© The Regents of the University of California

§6.43 e. Supplemental Property Tax Bill

The seller of residential real property containing one to four dwelling units, or the seller's agent, must provide a written notice to a prospective buyer advising that the buyer may receive one or more "supplemental property tax bills" based on the revaluation of the property after the transfer of ownership. CC §1102.6c. The notice must also state that the supplemental tax bills are not mailed to the buyer's lender and that payment is the responsibility of the buyer-taxpayer. Section 1102.6c specifies the language and font size of the required notice.

© The Regents of the University of California

§6.44 f. Former Federal or State Ordnance Locations

The seller of residential real property who has actual knowledge of any former federal or state ordnance locations within one mile of the property must give written notice of that knowledge to the buyer as soon as possible before the transfer of title. CC §1102.15. A former federal or state ordnance location is defined as an area identified by federal or state government as having once been used for military training purposes that may contain potentially explosive munitions. CC §1102.15.

© The Regents of the University of California

§6.45 g. Window Security Bars and Safety Release Mechanisms

Sellers must disclose, on the TDS form or the Local Option TDS form, the existence of any window security bars and any safety release mechanisms on them. CC §1102.16. Written disclosures of the existence of safety release mechanisms on security window bars may also be included in existing transactional documents, such as a real estate sales contract or receipt for deposit. Health & S C §17958.4.

© The Regents of the University of California

§6.46 h. Industrial Use Zone

If the seller has actual knowledge that the property is adjacent to or zoned to allow an industrial use described in CCP §731a, or is affected by a nuisance created by such industrial use, the seller must give written notice of such knowledge to the buyer before transfer of title. CC §1102.17. An industrial use zone is an area established by a city or county where certain manufacturing, commercial, or airport uses are expressly permitted. CCP §731a. An industrial use within a zone or district that has been lawfully established is deemed a nuisance only when "unnecessary and injurious methods of operation" are used, excluding, however, the regulation and working hours of canneries, fertilizing plants, refineries, "and other similar establishments" that produce offensive odors. CCP §731a.

© The Regents of the University of California

§6.46A i. Private Transfer Fees

As of January 1, 2008, when delivering the transfer disclosure statement, sellers must disclose to buyers whether the property is subject to a private transfer fee imposed by a covenant, condition, or restriction contained in a deed, contract, security interest, or other document affecting the transfer or sale of the property (or any interest in the property). The disclosure statement must include:

- Notice that payment of the transfer fee is required;
- The amount of the fee based on the asking price of the property and how the fee is calculated;
- Notice that the final amount of the fee may be different if it is calculated on the basis of a percentage of the final sale price;
- The entity to which the fee will be paid;
- The purposes of the fee; and
- The date or circumstances under which the obligation to pay the transfer fee expires.

CC §1102.6e. The definition of "transfer fee" in CC §1098 excludes, among other things, authorized assessments, charges, fees, and penalties imposed in connection with the transfer of a separate interest in a common interest development. On disclosure of transfer fees, see Advising California Common Interest Communities, chap 2 (Cal CEB 2003).

© The Regents of the University of California

§6.47 2. Natural Hazard Disclosures

Certain disclosures of natural hazards must be made in every transaction in which a transfer disclosure is required. CC §1103. (For a general discussion of transfer disclosures, see §6.35.) In addition, natural hazard disclosures must be made in two types of transactions that are exempt from the transfer disclosure requirements: (1) a transaction that requires a subdivision public report (or that can be made without one under Bus & P C §11010.4) and (2) foreclosure of a security interest in a manufactured home or mobilehome. CC §1103.1.

The same standards and requirements that apply to transfer disclosures in general are restated in, and apply to, natural hazard disclosures:

- A waiver of the disclosure requirement is void as against public policy. CC §1103(d).
- The disclosure must be made in good faith. CC §1103.7.
- The disclosures must be delivered personally or by mail to the transferee or transferee's spouse or real estate agent. CC §§1103.10-1103.11.
- Delivery must made as soon as practicable before transfer of title or execution of the contract, and the transferor must indicate compliance in writing. CC §1103.3(a)-(b).
- If the disclosures or material amendments to them are delivered after the purchase offer is executed, then the buyer has a right of rescission. CC §1103.3(c).
- The seller has qualified liability protection for erroneous disclosures. CC §1103.4(a).
- Certain substitute disclosures are authorized. CC §1103.4(b).
- Compliance discharges further disclosure duties with respect to the same subject matter, except the duty to disclose known material facts. CC §§1103.5(a), 1103.8.
- A disclosure subsequently rendered inaccurate as a result of changed circumstances is not a violation. CC §1103.5(b).
- Noncompliance does not invalidate a transfer, but if noncompliance is willful or negligent, the transferor is liable for actual damages suffered by transferee. CC §1103.13.

© The Regents of the University of California

§6.48 a. Natural Hazard Zones

In every transaction in which a natural hazard disclosure must be made (see §6.47), the transferor or the transferor's agent must disclose to the transferee whether the property is located in one or more of the following six "natural hazard" zones (see CC §1103(c)) when such disclosure is required by statute:

- A "special flood hazard area" as designated by the Federal Emergency Management Agency (FEMA) (see Govt C §8589.3);
- An area of potential flooding designated under Govt C §8589.5 (see Govt C §8589.4);
- A very high fire hazard severity zone that is subject to the maintenance requirements of Govt C §51182, as identified by the State Director of Forestry and Fire Protection under Govt C §51178 (see Govt C §51183.5);
- An earthquake fault zone designated by the State Geologist under the Alquist-Priolo Earthquake Fault Zoning Act (Pub Res C §§2621-2630) (see Pub Res C §2621.9);
- A seismic hazard zone designated under Pub Res C §2696 (see Pub Res C §2694); and
- A state responsibility area, *e.g.,* a wildland area that may contain substantial forest fire risks and hazards, as determined under Pub Res C §4125 (see Pub Res C §4136).

As between the transferor and its agent, the transferor is responsible for making the "very high fire severity zone" disclosure and "state responsibility area" disclosure. The transferor's agent is responsible for making the other disclosures, but if the transferor is acting without an agent, the transferor is responsible. CC §1103(c).

Disclosure is required under CC §1103(c) in the following circumstances:

- If the transferor or agent has actual knowledge of the property's location within a natural hazard zone;
- If the local jurisdiction has compiled and posted notice in certain county offices of a list of properties that are located within the zone; or
- When a map of such properties has been provided to the local jurisdiction by the designated state agency, if the local jurisdiction has posted notice of the location of the map and any information regarding changes to it received by the local agency.

In transfers not subject to the natural hazard disclosure requirements, the transferor or agent may make the required disclosures in a separate writing. CC §1103.1(b).

© The Regents of the University of California

§6.49 b. Natural Hazard Disclosure Statement

The natural hazard disclosures must be made on the statutorily mandated Natural Hazard Disclosure Statement (NHDS) form set forth in CC §1103.2. For the California Association of Realtors® form, see §6.50. The disclosure may also be made on the Local Option Real Estate Disclosure Statement described in CC §1102.6a (see §6.39) as long as it includes substantially the same information and warnings as required on the NHDS form. CC §1103.2(e). The NHDS form states that the disclosures are not a warranty and are not intended to be part of the parties' contract, and further states that the hazards disclosed may limit the transferee's ability to develop the property, obtain insurance, or receive assistance after a disaster. CC §1103.2.

As in the case of other transfer disclosures (except those made by the transferor and agents in the TDS), it is now standard practice for the transferor to contract with a third party "expert" disclosure company, for a modest fee, to make the natural hazard disclosures. When such substitute disclosure is used, three additional disclosure requirements are imposed. First, the expert must determine whether the property is located within an "airport influence area" as defined in Bus & P C §11010, and if so, a statutorily mandated Notice of Airport in Vicinity must be given to the transferee. CC §1103.4(c)(1). Second, the expert must determine whether the property is located within the jurisdiction of the San Francisco Bay Conservation and Development Commission as defined in Govt C §66620, and if so, a statutorily mandated Notice of San Francisco Bay Conservation and Development Commission Jurisdiction must be given to the transferee. CC §1103.4(c)(2). Third, the expert must determine whether the property is located within one mile of a farm or ranch land designated by the California Department of Conservation, Division of Land Resource Protections, and if so, a statutorily mandated "Notice of Right to Farm" must be given to the transferee. CC §1103.4(c)(3).

The Natural Hazard Disclosure Statement is a disclosure between the transferor and agent, on the one hand, and the transferee, on the other, and may not be used for any purpose by any third party, including lenders, insurers, and governmental agencies. CC §1103.2(g).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/6 Residential Purchase and Sale Transactions/ §6.50 c. Form: Natural Hazard Disclosure Statement (CAR Form NHD)

§6.50 c. Form: Natural Hazard Disclosure Statement (CAR Form NHD)

Print

CALIFORNIA ASSOCIATION OF REALTORS®

NATURAL HAZARD DISCLOSURE STATEMENT

(C.A.R. Form NHD, Revised 10/04)

This statement applies to the following property: _____

The transferor and his or her agent(s) or a third-party consultant disclose the following information with the knowledge that even though this is not a warranty, prospective transferees may rely on this information in deciding whether and on what terms to purchase the subject property. Transferor hereby authorizes any agent(s) representing any principal(s) in this action to provide a copy of this statement to any person or entity in connection with any actual or anticipated sale of the property.

The following are representations made by the transferor and his or her agent(s) based on their knowledge and maps drawn by the state and federal governments. This information is a disclosure and is not intended to be part of any contract between the transferee and transferor.

THIS REAL PROPERTY LIES WITHIN THE FOLLOWING HAZARDOUS AREA(S):

A SPECIAL FLOOD HAZARD AREA (Any type Zone "A" or "V") designated by the Federal Emergency Management Agency.

Yes _____ No _____ Do not know and information not available from local jurisdiction _____

AN AREA OF POTENTIAL FLOODING shown on a dam failure inundation map pursuant to Section 8589.5 of the Government Code.

Yes _____ No _____ Do not know and information not available from local jurisdiction _____

A VERY HIGH FIRE HAZARD SEVERITY ZONE pursuant to Section 51178 or 51179 of the Government Code. The owner of this property is subject to the maintenance requirements of Section 51182 of the Government Code.

Yes _____ No _____

A WILDLAND AREA THAT MAY CONTAIN SUBSTANTIAL FOREST FIRE RISKS AND HAZARDS pursuant to Section 4125 of the Public Resources Code. The owner of this property is subject to the maintenance requirements of Section 4291 of the Public Resources Code. Additionally, it is not the state's responsibility to provide fire protection services to any building or structure located within the wildlands unless the Department of Forestry and Fire Protection has entered into a cooperative agreement with a local agency for those purposes pursuant to Section 4142 of the Public Resources Code.

Yes _____ No _____

AN EARTHQUAKE FAULT ZONE pursuant to Section 2622 of the Public Resources Code.

Yes _____ No _____

A SEISMIC HAZARD ZONE pursuant to Section 2696 of the Public Resources Code.

Yes (Landslide Zone) _____ Yes (Liquefaction Zone) _____

No _____ Map not yet released by state _____

SAMPLE

The copyright laws of the United States (Title 17 U.S. Code) forbid the unauthorized reproduction of this form, or any portion thereof, by photocopy machine or any other means, including facsimile or computerized formats. Copyright © 1998-2004, CALIFORNIA ASSOCIATION OF REALTORS®, INC. ALL RIGHTS RESERVED.

Buyer's Initials (_____)(_____)
Seller's Initials (_____)(_____)

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

Print

Property Address: _____ Date: _____

THESE HAZARDS MAY LIMIT YOUR ABILITY TO DEVELOP THE REAL PROPERTY, TO OBTAIN INSURANCE, OR TO RECEIVE ASSISTANCE AFTER A DISASTER.

THE MAPS ON WHICH THESE DISCLOSURES ARE BASED ESTIMATE WHERE NATURAL HAZARDS EXIST. THEY ARE NOT DEFINITIVE INDICATORS OF WHETHER OR NOT A PROPERTY WILL BE AFFECTED BY A NATURAL DISASTER. TRANSFEREE(S) AND TRANSFEROR(S) MAY WISH TO OBTAIN PROFESSIONAL ADVICE REGARDING THOSE HAZARDS AND OTHER HAZARDS THAT MAY AFFECT THE PROPERTY

Signature of Transferor(s) _____ Date _____

Signature of Transferor(s) _____ Date _____

Agent(s) _____ Date _____

Agent(s) _____ Date _____

Check only one of the following:

☐ Transferor(s) and their agent(s) represent that the information herein is true and correct to the best of their knowledge as of the date signed by the transferor(s) and agent(s).

☐ Transferor(s) and their agent(s) acknowledge that they have exercised good faith in the selection of a third-party report provider as required in Civil Code Section 1103.7, and that the representations made in this Natural Hazard Disclosure Statement are based upon information provided by the independent third-party disclosure provider as a substituted disclosure pursuant to Civil Code Section 1103.4. Neither transferor(s) nor their agent(s) (1) has independently verified the information contained in this statement and report or (2) is personally aware of any errors or inaccuracies in the information contained on the statement. This statement was prepared by the provider below:

Third-Party Disclosure Provider(s) _____ Date _____

Transferee represents that he or she has read and understands this document. Pursuant to Civil Code Section 1103.8, the representations made in this Natural Hazard Disclosure Statement do not constitute all of the transferor's or agent's disclosure obligations in this transaction.

Signature of Transferee(s) _____ Date _____

Signature of Transferee(s) _____ Date _____

SAMPLE

The copyright laws of the United States (Title 17 U.S. Code) forbid the unauthorized reproduction of this form, or any portion thereof, by photocopy machine or any other means, including facsimile or computerized formats. Copyright © 1998-2004, CALIFORNIA ASSOCIATION OF REALTORS®, INC. ALL RIGHTS RESERVED.

THIS FORM HAS BEEN APPROVED BY THE CALIFORNIA ASSOCIATION OF REALTORS® (C.A.R.). NO REPRESENTATION IS MADE AS TO THE LEGAL VALIDITY OR ADEQUACY OF ANY PROVISION IN ANY SPECIFIC TRANSACTION. A REAL ESTATE BROKER IS THE PERSON QUALIFIED TO ADVISE ON REAL ESTATE TRANSACTIONS. IF YOU DESIRE LEGAL OR TAX ADVICE, CONSULT AN APPROPRIATE PROFESSIONAL.

This form is available for use by the entire real estate industry. It is not intended to identify the user as a REALTOR®. REALTOR® is a registered collective membership mark which may be used only by members of the NATIONAL ASSOCIATION OF REALTORS® who subscribe to its Code of Ethics.

SURE TRAC The System for Success®

Published and Distributed by:
REAL ESTATE BUSINESS SERVICES, INC.
a subsidiary of the California Association of REALTORS®
525 South Virgil Avenue, Los Angeles, California 90020

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

NATURAL HAZARD DISCLOSURE STATEMENT (NHD PAGE 2 OF 2)

Comment: This form is reprinted with the permission of the California Association of Realtors®. Endorsement is not implied.

© The Regents of the University of California

3. Health and Safety Disclosures

§6.51 a. Lead-Based Paint Disclosure

Under the federal Residential Lead-Based Paint Reduction Act of 1992 (42 USC §§4851-4856) and implementing regulations (40 CFR §§745.100-745.119), before a buyer or lessee becomes obligated to purchase or lease a single-family or multi-unit dwelling that was built before 1978 and is used or will be used for residential purposes, the seller, the lessor, or the real estate agent (if any) must do all of the following (42 USC §4852d(a)(1)):

- Provide the buyer or lessee with a lead hazard information pamphlet prescribed by the Administrator of the Environmental Protection Agency, entitled "Protect Your Family From Lead in Your Home";
- Disclose to the buyer or lessee the presence of any known lead-based paint or lead-based paint hazards and provide any available lead hazard evaluation report; and
- Allow the buyer a 10-day period (unless the parties mutually agree to a different period) to conduct a risk assessment or inspection for lead-based paint hazards.

In addition, the purchase agreement must contain a prescribed Lead Warning Statement and a statement signed by the purchaser stating that he or she has read the statement and understands it, has received the required pamphlet, and has had the 10-day opportunity (or alternative mutually acceptable period) to conduct lead hazard inspections. 42 USC §4852d(a)(2)-(3).

The following types of housing are exempt from the law:

- Housing built on or after January 1, 1978, with certain exceptions (40 CFR §745.103);
- "Zero bedroom" units, including efficiencies, lofts, and dormitories (40 CFR §745.103);
- Housing sold at foreclosure sale (40 CFR §745.101(a));
- Short-term leases for less than 100 days without option to extend or renew (which would not include month-to-month tenancies) (40 CFR §§745.101(c)); and
- Housing otherwise covered that has been found to be lead free by a certified inspector (40 CFR §745.101(b)).

Failure to comply with the Act will not invalidate or render unenforceable any purchase contract, lease, or loan, or create a title defect. 42 USC §4852d(c). Knowing violations of the Act by sellers, lessors, and agents, however, subject them to civil monetary penalties and joint and several liability for three times the damages incurred by the purchaser or lessee plus attorney fees and costs, as well as injunctive relief and criminal penalties. 42 USC §4852d(b); see *Smith v Coldwell Banker Real Estate Servs.* (D Conn 2000) 122 F Supp 2d 267, 273 (a "knowing" violation of the Act does not require a showing of bad faith or willfulness).

PRACTICE TIP: The lead disclosure requirements may be satisfied by completing CAR Form FLD and by delivering to the purchaser CAR's publication entitled "Environmental Hazards: Guide for Homeowners and Buyers." The Act requires disclosure only and does not require a seller to test for lead or abate known lead paint or hazards at a property.

© The Regents of the University of California

§6.52 b. Earthquake Hazards

For residential real property built before January 1, 1960, comprising one to four living units of conventional light-frame construction (as defined in Uniform Building Code §2320.11.3) the transferor must, as soon as practicable before the transfer, (1) deliver to the transferee a copy of the pamphlet entitled "Homeowner's Guide to Earthquake Safety" (Homeowner's Guide) published by the Seismic Safety Commission under Bus & P C §10149; and (2) complete an earthquake hazards report disclosing the transferor's actual knowledge of whether the property has any of the deficiencies listed in Govt C §8897.2(a). Govt C §8897.1(a). These include the absence of anchor bolts, the existence of unbraced perimeter cripple walls, unbraced first-story walls, a perimeter foundation composed of unreinforced masonry, unreinforced masonry dwelling walls, a habitable room above a garage, or an unbraced water heater. Govt C §8897.2(a). The Homeowner's Guide includes a Residential Earthquake Hazards Report form, which is typically completed by the transferor to satisfy this disclosure requirement. The transferor must also disclose any actual knowledge regarding corrective measures taken to address any of the above deficiencies. Govt C §8897.2(b).

In addition, for any unreinforced masonry building with wood-frame floors or roofs built before January 1, 1975, the transferor must, as soon as practicable before the transfer, deliver to the transferee a copy of another pamphlet, entitled "Commercial Property Owner's Guide to Earthquake Safety" (Commercial Guide), published by the Seismic Safety Commission under Bus & P C §10147.

Exemptions are essentially the same as those that apply to the TDS and NHDS (see §6.35), with the additional exemption of transfers in which the transferee has agreed in writing to demolish the dwelling within 1 year of the date of transfer. Govt C §§8897.1(c), 8893.3(j).

If the Homeowner's Guide or Commercial Guide is delivered to a transferee, the transferor is not required to provide any additional information about geologic and seismic hazards in general, and the information in the guides will be deemed sufficient to inform the transferee about such hazards. CC §2079.8(a). Delivery of the guides, however, does not alter the transferor's duties under the transfer disclosure and natural hazard disclosure laws or the duty to disclose the existence of known hazards. CC §2079.8(b).

PRACTICE TIP: Delivery of the Homeowner's Guide and the Residential Earthquake Hazard Report is advisable in all residential transactions, even if not mandatory, because the protections in CC §2079.8(a) are not limited to transactions in which the Guide and Report are mandatory.

© The Regents of the University of California

c. Environmental Hazards

§6.53 (1) Mandatory Disclosure

The only mandatory state disclosure requirement pertaining to environmental hazards is found in the TDS. (See §6.51 for discussion of the federal lead hazard disclosure requirements.) The TDS (Part II.C.1) requires the transferor to disclose any known "substances, materials, or products which may be an environmental hazard"; specific examples include asbestos, formaldehyde, radon gas, lead-based paint, mold, fuel or chemical storage tanks, and contaminated soil or water. See §6.36. See also chap 7 for a discussion of hazardous waste aspects of real property sale transactions. Actual knowledge of the presence of any of the items enumerated in the TDS must be disclosed. In addition, a seller must consider whether any substance, material, or product present at the property, other than those specifically enumerated on the TDS, "may be an environmental hazard," and if so, disclose it. See §§6.35-6.36.

EXAMPLE: Spray-on acoustical ("popcorn" or "cottage cheese") ceilings and pipe and duct wrapping of a certain age (generally pre-1988) and appearance may contain asbestos. If the seller does not know whether these materials in his or her home contain asbestos, but knows they may, it would be most prudent either to disclose the materials and disclaim any knowledge of their contents, or have the materials tested and disclose the results of the tests. The presence of suspected asbestos-containing materials should also be noted in a competent home inspection report.

NOTE: There are currently no statutory mold disclosure requirements in California. Although the state legislature has enacted comprehensive mold legislation known as the Toxic Mold Protection Act of 2001 (Health & S C §§26100-26157), which amended the TDS form to add "mold" to the list of environmental hazards, the disclosure requirements of the Act do not take effect until after the California Department of Public Health (CDPH) has adopted standards and guidelines for permissible exposure limits (PELs), assessing health threats from mold spores, and remediation of indoor mold. Health & S C §26140(d). In April 2005, CDPH staff released a report concluding that sound, science-based PELs for indoor molds could not be established at that time. A July 2008 CDPH update restates that conclusion. Thus, it is uncertain if and when the Act's disclosure requirements will take effect.

Local ordinances should also be consulted for any environmental matters that should be disclosed.

EXAMPLE: Under the City and County of San Francisco Health Code, if a real property owner has reason to believe that an abandoned underground storage tank (UST) is located under the property, or the immediately adjacent sidewalk or public street, the owner must make a reasonable effort to locate the UST, and if located, submit a plan to close or update, register, or permit the UST. SF Health C, art 21, §1153. San Francisco sellers customarily disclose this requirement to buyers and provide buyers with a written report by a qualified licensed contractor, stating that no USTs have been located. Absent delivery of such a report, buyers should obtain a professional inspection for USTs before the close of escrow.

© The Regents of the University of California

§6.54 (2) Voluntary Disclosure

The seller and broker can partially satisfy their disclosure duties regarding environmental hazards by providing the transferee with a copy of the consumer booklet "Residential Environmental Hazards: A Guide For Homeowners, Homebuyers, Landlords and Tenants," published by the California Department of Toxic Substances Control. The booklet generally covers the hazards enumerated in the TDS as well as "household hazardous waste." Bus & P C §10084.1. Upon delivery of the booklet to the transferee, the seller and broker will have satisfied the disclosure requirement regarding the common household environmental hazards described in the booklet, and the transferee is deemed to have been adequately informed on the subject. CC §2079.7(a). However, the seller and agent must still disclose any known environmental hazards on or affecting the real property. CC §2079.7(b).

© The Regents of the University of California

§6.55 d. Drug Lab Cleanup Order

The Methamphetamine Contaminated Property Cleanup Act of 2005 (Health & S C §§25400.10-25400.47) requires local officials, upon determining that a property has been contaminated from the manufacture or storage of methamphetamines, to issue a cleanup order to the property owner. See Health & S C §25400.22. Until the owner receives a notice from the local health official that no further cleanup action is required, the owner must provide written notice and a copy of the order to a prospective buyer, who must acknowledge receipt in writing. Health & S C §25400.28(a).

© The Regents of the University of California

§6.56 e. Registered Sex Offenders ("Megan's Law")

"Megan's Law" statutes require law enforcement agencies to make available to the public information about registered sex offenders, including their identity, location, and criminal history. See 42 USC §§14071-14073 and final guidelines at 62 Fed Reg 39009 (1997); Pen C §§290.4, 290.45, 290.46. Every contract for the sale of residential real property comprising one to four dwelling units entered into after July 1, 1999, must contain a specified statutory notice regarding access to the database of registered sex offenders maintained by the Department of Justice. CC §2079.10a. The content of the notice differs depending on when the parties entered into the purchase agreement. See CC §2079.10a(a)(3) (required notice language for contracts entered into on or after April 1, 2006).

NOTE: The Megan's Law notice language is incorporated into the CAR California Residential Purchase Agreement and Joint Escrow Instructions, ¶5.C (see §6.24). See CC §2079.10a(1).

On delivery of the required notice, the seller, lessor, or broker is not required to provide additional information regarding the proximity of registered sex offenders; however, compliance with the notice requirement does not alter any existing duty of disclosure under other statutes or case law. CC §2079.10a(b)-(c). Delivery of the notice does not give rise to a cause of action by the registered sex offender against the disclosing party. CC §2079.10a(b).

© The Regents of the University of California

§6.57 f. Smoke Detector Compliance Statement

In California, all dwelling units intended for human occupancy must have operable smoke detectors that have been approved and listed by the State Fire Marshal and installed in accordance with the Fire Marshal's regulations. Health & S C §§13113.7-13113.8. Local ordinances requiring smoke detectors in single-family dwellings may be enacted as long as they satisfy statutory minimum requirements. Health & S C §13113.8(h).

Before the transfer of a single-family dwelling, the seller must deliver to the buyer, in the purchase contract or the addendum or in a separate document, a written statement that the property complies with the statutory smoke detector requirements. Health & S C §13113.8(b). Delivery must be in-person or by mail to the buyer or his or her spouse, unless the purchase contract provides otherwise, or to the buyer's authorized agent in the transaction. Health & S C §13113.8(c). CAR Form WHSD can be used to satisfy this requirement. Exceptions to the smoke detector compliance statement requirement are set forth in §13113.8(d) and essentially track the exemptions set forth in CC §1102.2 (discussed in §6.35). The failure to deliver a compliance statement does not invalidate a transfer of title; rather, the exclusive remedy is an award of actual damages not to exceed $100, exclusive of attorney fees and costs. Health & S C §13113.8(g).

PRACTICE TIP: Although the statute requires delivery of a compliance statement only in the sale of a "single-family dwelling," the substantive smoke detector requirements apply to all types of residential dwellings, and the compliance statement is typically given voluntarily by sellers of condominiums and other residential property interests.

© The Regents of the University of California

§6.58 g. Water Heater Compliance Statement

All existing residential water heaters, and new and replacement water heaters sold in California, must be braced, anchored, or strapped, to resist falling or horizontal displacement caused by earthquake motion, in accordance with the requirements of the California Plumbing Code or local modifications to it. Health & S C §19211(a). "Water heater" is defined to include those with a capacity of not more than 120 gallons for which a pre-engineered strapping kit is readily available. Health & S C §19211(d). The Division of the State Architect has published "Guidelines for Earthquake Bracing of Residential Water Heaters," which is available on the Publications page of the State Architect's website. See the Directory for the address.

A seller of real property that contains a water heater must certify to a prospective buyer in writing that the water heater complies with this law. Health & S C §19211(b). There are no exemptions. CAR Form WHSD may be used to comply with this law.

© The Regents of the University of California

§6.59 h. Structural Pest Control Inspection Report

There is no statutory requirement that a seller obtain and deliver to the buyer a structural pest control inspection report prepared under Bus & P C §8516. When the purchase agreement or lender requires such a report as a condition of the transfer or financing, however, the seller or agent must deliver a copy of the report to the buyer as soon as practicable before the transfer of title. CC §1099(a). Delivery may be in-person or to the buyer or his or her spouse or agent. CC §1099(c). A seller's failure to comply with §1099 will not invalidate the transfer of title unless the seller's conduct would be a valid ground for rescission absent the statute. CC §1099(d). If the seller obtains more than one pest control inspection report, copies of all such reports must be delivered to the buyer. *Godfrey v Steinpress* (1982) 128 CA3d 154, 173, 180 CR 95.

© The Regents of the University of California

§6.60 4. Common Interest Development Disclosures

Three statutory disclosure requirements apply to the sale of separate interests in common interest developments (CIDs), including condominiums, stock cooperatives, community apartment projects, and planned developments:

- For all transactions involving CIDs, required disclosures are set forth in the Davis-Stirling Common Interest Development Act (Davis-Stirling Act) (CC §§1350-1378). CC §1368. See §6.61.
- For transactions involving the sale of newly converted condominiums, required disclosures are set forth in CC §1134. See §6.62.
- For transactions involving the sale of units in a new CID project, required disclosures are set forth in Bus & P C §11018.6. See §6.63.

For further information on common interest developments, see Forming California Common Interest Developments (Cal CEB 2004); Advising California Common Interest Communities (Cal CEB 2003).

© The Regents of the University of California

§6.61 a. Davis-Stirling Act Disclosures

Under CC §1368, the owner of a separate interest in a CID must make extensive disclosures of the following information and documents to a prospective buyer as soon as practicable before transfer of title (CID disclosures):

- A copy of the CID's "governing documents," including the declaration (*i.e.,* CC&Rs), articles of incorporation (or an authorized statement that the association is unincorporated), bylaws, operating rules, and any other documents governing the operation of the CID or the association that manages it (CC §1368(a)(1));
- If the CID is age-restricted in a manner not authorized by CC §51.3 ("senior citizen" housing), a statement that the restriction is enforceable only to the extent permitted by CC §51.3 (CC §1368(a)(2));
- A copy of the CID's operating budget, summary of reserves, insurance, and other financial documents and information prepared and distributed by the association to its members in accordance with CC §1365 (CC §1368(a)(3));
- A statement from an authorized representative of the association of current assessment amounts, any unpaid assessments, monetary fines or penalties levied on the owner's unit, and any late charges, interest, or costs that may become a lien on the owner's interest in the CID (CC §1368(a)(4));
- A copy or summary of any unresolved notice of violation of the governing documents sent to the owner (CC §1368(a)(5));
- A copy of any initial list of construction defects prepared in accordance with CC §1375, unless the association and builder have settled and the association has complied with the post-settlement disclosure requirements of §1375.1, in which case such disclosures must be made (CC §1368(a)(6)-(7)); and
- Any changes in the association's assessments that have been approved but are not yet due and payable (CC §1368(a)(8)).

Homeowners' associations are required, within 10 days of receiving a written request, to provide the owner with a copy of all of the above documents, and may charge a reasonable fee based on the association's actual cost to comply with the request. CC §1368(b). This is the extent of the homeowners' association's legal obligation in connection with CID disclosures. The association does not owe a disclosure duty to the potential purchaser of a separate interest in a CID. See *Kovich v Paseo Del Mar Homeowners' Ass'n* (1996) 41 CA4th 863, 866, 48 CR2d 758 (association has no duty to disclose construction defects to potential purchaser of condo).

A failure to comply with the requirements of §1368 does not invalidate transfer of title. A person who willfully violates §1368, however, is liable to the purchaser of the separate interest for actual damages, a civil penalty not to exceed $500, and attorney fees. CC §1368(d)-(e).

© The Regents of the University of California

§6.62 b. Disclosures in First Sale of Conversion Units

When an existing dwelling has been converted to a condominium, stock cooperative, or community apartment project, the owner or subdivider, before transfer of title for the first sale of a unit and after performing a reasonable inspection, must deliver to a prospective buyer a written statement that either lists all substantial defects or malfunctions in the major systems in the unit and the common areas of the project or disclaims any knowledge of any such defect or malfunction. CC §1134(a).

As with the Transfer Disclosure Statement (see §6.35), if the statement is delivered after the buyer has executed a purchase contract, the buyer has 3 days after personal delivery of the statement, or 5 days after delivery by deposit in the mail, to rescind the purchase contract in writing. If delivered after the contract is executed, the statement must include a statement of the buyer's right, method, and time to rescind. CC §1134(b).

The written statement is not intended to abridge or limit other applicable disclosure obligations. CC §1134(g). Failure to comply with §1134 will not invalidate a transfer of title. CC §1134(f). A person who willfully violates §1134, however, is liable for actual damages suffered by the buyer. CC §1134(d). In addition, the injured party may pursue any other available legal remedies. CC §1134(e).

© The Regents of the University of California

§6.63 c. Disclosures in First Sale of Units in a New Common Interest Development

In the case of a new common interest development (CID) for which a public report is required, the seller of the separate interests must allow a potential buyer to review the following (and must give an actual buyer copies as early as possible in advance of the title transfer): the governing documents for the subdivision, current financial information and related statements specified in CC §1365(a) to the extent they are available (see §6.61), and a statement of outstanding delinquent accounts. Bus & P C §11018.6. In addition, when the public report is delivered, the developer must also give the potential buyer the detailed statement of general information about CIDs specified in Bus & P C §11018.1(c).

© The Regents of the University of California

§6.64 5. New Home Sales Disclosures

Residential dwellings built after January 1, 2003, are subject to certain minimum standards for residential construction. CC §896. For example, builders of such homes must provide a minimum 1-year express written limited warranty covering the fit and finish of certain specified building components. CC §900. In addition, detailed alternative dispute resolution (ADR) and other pre-litigation procedures govern the resolution of construction defect disputes involving such homes. CC §§910-945.5. (For a thorough discussion of construction defect actions from the developer's perspective, see Forming California Common Interest Developments §§8.30-8.63 (Cal CEB 2004); for a discussion from the homeowner associations' perspective, see Advising California Common Interest Communities §§10.25-10.41 (Cal CEB 2003).)

Under CC §912, a builder must provide the following information and documents to a new home buyer "in conjunction with the initial sale of the residence" and thereafter within 30 days of service of a written request for documents at the homeowner's expense:

- Copies of all maintenance and preventive maintenance recommendations that pertain to the homeowner's residence (CC §912(b));
- Copies of all manufactured products maintenance, preventive maintenance, and limited warranty information (CC §912(c));
- Copies of all of the builder's limited contractual warranties in effect at the time of the original sale (CC §912(d));
- Disclosure (by recording on title) of the ADR and pre-litigation procedures established by CC §§910-938, with a statement that these procedures affect homeowners' legal rights (CC §912(f));
- A written copy of CC §§895-945.5 (CC §912(g)); and
- An instruction to the homebuyer that he or she must provide subsequent buyers with "any documents provided in conjunction with the original sale" (CC §912(h)).

A builder who fails to timely comply with any of the above requirements is not entitled to the protection of CC §§895-945.5, and the homeowner may pursue an action against the builder without having to comply with the ADR and other pre-litigation procedures in the law. CC §912(i).

© The Regents of the University of California

6. Miscellaneous Disclosures

§6.65 a. Death or Illness of Occupant of Property

To address uncertainty about a seller's and broker's obligation, if any, to disclose the death of an occupant of residential property, or the fact that the occupant was afflicted with, or died from, the virus that causes AIDS, the legislature enacted CC §1710.2. The concern regarding disclosure of death at a property arose out of *Reed v King* (1983) 145 CA3d 261, 193 CR 130 (multiple murder that occurred at property 10 years before sale was material and had to be disclosed if it could be shown the murder significantly affected market value). The need to address AIDS disclosures arose out of what the legislature characterized in 1986 as "public fears or anxieties [regarding AIDS] approaching, in some circumstances, panic or hysteria." Stats 1986, ch 498, §1(b).

A seller or its agent will not be liable to a buyer for failing to disclose that an occupant died on the property, or the manner of death, if the death occurred more than 3 years before the date of the buyer's purchase offer, or that an occupant of the property had, or died from, the virus that causes AIDS. CC §1710.2(a). This liability protection does not modify any other disclosure obligation pertaining to physical or mental conditions or diseases (other than AIDS) or the physical condition of the property, and does not immunize a seller or agent who intentionally misrepresents the facts regarding a death at the property in response to a direct question from a prospective buyer. CC §1710.2(d).

If an occupant dies within 3 years before the date of the purchase offer from a cause *other than AIDS,* the death must be disclosed if it significantly affects market value. See *Reed,* 145 CA3d at 268. *Reed,* which was decided at the pleading stage, held that the issue of whether a particular death significantly affected the market value of a property must be proved with competent evidence and that, in deciding the question, the trier of fact may rely on expert opinion and common knowledge and experience. *Reed v King, supra.* To date, no published decision has considered whether death from a cause other than a multiple murder—such as death from a single murder or suicide or natural causes (including diseases other than AIDS)—would be material so as to require disclosure.

PRACTICE TIP: It is probably most prudent to disclose the death of an occupant that occurred within 3 years before a purchase offer, regardless of the cause of death (other than death from AIDS). This eliminates the need to evaluate materiality generally or under the specific facts of the transaction, and thus avoids exposure to liability. The seller should disclose the manner of death only if it is known. The seller has no duty to investigate an unknown cause of death.

© The Regents of the University of California

§6.66 b. Advisability of Title Insurance

In a transaction for the purchase or simultaneous exchange of real property for which title insurance will not be issued to the buyer or the parties to the exchange, a specified notice regarding the advisability of purchasing title insurance must be provided to, and signed and acknowledged by, the buyer or exchange parties. CC §1057.6. For a discussion of available title insurance, see California Title Insurance Practice (2d ed Cal CEB 1997).

© The Regents of the University of California

§6.67 c. FHA/HUD Inspection Disclosure

For every resale of residential real property containing one to four units that will involve Federal Housing Administration (FHA) mortgage insurance, the Department of Housing and Urban Development (HUD) requires the lender to deliver to the buyer a disclosure form entitled "For Your Protection: Get a Home Inspection" (Form HUD 92564-CN). See HUD Mortgagee Letters 99-18, 99-33, 06-24, available on the HUD website; see the Directory for the website address.

© The Regents of the University of California

§6.68 d. Flood Disaster Insurance Requirements

If a person has received federal flood disaster assistance on the condition that flood insurance be maintained, and the person fails to maintain such insurance, federal law prohibits the use of federal funds for the repair, replacement, or restoration of damage to that person's personal, residential, and commercial property. 42 USC §5154a(a). If such property is not insured, then on transfer of the property the transferor must give written notice to the transferee, in the transfer documents, of the requirement to obtain and maintain flood insurance on the property. 42 USC §5154a(b)(1). If the transferor fails to give the required notice and the transferee receives federal relief in a subsequent flood disaster, the transferor will be required to reimburse the federal government. 42 USC §5154a(b)(2).

© The Regents of the University of California

§6.69 e. Financing Disclosures

If a seller finances any portion of the buyer's purchase price for a property with up to four residential units, and the terms of the financing are negotiated or arranged by a third person who receives direct or indirect compensation for doing so, the credit arranger must provide to the buyer and seller—and the parties must provide to each other—written disclosure of certain information within their personal knowledge. CC §2956. The matters that must be disclosed include identification of the note and security and various warnings regarding the dangers of such financing. CC §2963. Attorneys representing any of the parties to the credit transaction are exempt from the disclosure requirements. CC §2957(a)(1). Disclosure is not required when the buyer is entitled to receive a disclosure under the Federal Truth in Lending Act (15 USC §1604), the Real Estate Settlement Procedures Act (RESPA) (12 USC §2601), or Bus & P C §10240. CC §2958.

If the loan is made for more than 1 year, is secured by a deed of trust on property with one to four residential units, and has a balloon payment at the end of the loan term, the holder of the note must comply with CC §2966 by sending to the borrower, 90 to 150 days before the loan is due, a statement that includes the following:

- The name and address of the person to whom the balloon payment is to be made (CC §2966(a)(1));
- The due date of the balloon payment (CC §2966(a)(2));
- The exact amount of the balloon payment or, if unknown, a good faith estimate of the amount (CC §2966(a)(3)); and
- A statement that the borrower has a contractual right to refinance the final payment, when the borrower has such a right (CC §2966(a)(4)).

© The Regents of the University of California

§6.70 f. Home Energy Rating Program

Public Resources Code §25402.9 requires the State Energy Commission to publish an informational booklet about the statewide home energy rating program adopted under Pub Res C §25942. When the booklet becomes available, a transferor who delivers a copy of the booklet to the transferee will not be required to provide additional information to the transferee about home energy ratings, and the booklet will be deemed sufficient to inform the transferee on the subject matter. CC §2079.10. As with other such consumer information booklets and guides, delivery of the booklet by the transferor does not alter the duty of disclosure under any other law. CC §2079.10(b).

NOTE: Federal law requires sellers of newly constructed homes and units to disclose the type, thickness, and R-value of insulation installed or to be installed in all parts of the house. 16 CFR §460.16.

© The Regents of the University of California

§6.71 IV. BUYER'S DUE DILIGENCE

The seller's disclosures are primarily intended to provide a buyer with information on material aspects of the transaction that are known to or accessible only to the seller and not known to or within the diligent attention or observation of the buyer. See §6.30. Conversely, buyers must act with reasonable care or "due diligence" in a transaction to protect their own interests, which includes discovering matters that are obvious and patent and investigating the details regarding facts disclosed by the seller. See §§6.72-6.77.

© The Regents of the University of California

§6.72 A. Buyer's Duty of Self-Protection

A buyer has a duty to exercise reasonable care to protect himself or herself in a real estate transaction. In *Easton v Strassburger* (1984) 152 CA3d 90, 103, 199 CR 383, which established the duty of the seller's agent to investigate and disclose reasonably discoverable defects to the buyer, the court noted that the agent's duty does not relieve a buyer of its own duty "to exercise reasonable care to protect himself." Although *Easton* cited no authority for such a buyer's duty, in 1985 the legislature codified *Easton*'s holding in CC §§2079-2079.24*,* which it characterized as declarative of the common law. CC §2079.12(a)(4). The agent's duty of disclosure does not relieve "a buyer or prospective buyer of the duty to exercise reasonable care to protect himself or herself, including [the duty to investigate] those facts which are known to or within the diligent attention and observation of the buyer or prospective buyer." CC §2079.5. Whether the buyer reasonably protected himself or herself is an issue of fact that depends on all the circumstances of the case. *Furla v Jon Douglas Co.* (1998) 65 CA4th 1069, 1079, 76 CR2d 911.

Before the enactment of CC §2079.5, it was well established that a buyer will be deemed to be aware of matters that are within his or her diligent attention and observation and conditions that are obvious and patent. 65 CA4th at 1079, citing *Tarrant v Butler* (1960) 180 CA2d 235, 4 CR 230. Whether a condition is obvious and patent is a question of fact. 180 CA2d at 240; *Sanfran Co. v Rees Blow Pipe Mfg. Co.* (1959) 168 CA2d 191, 202, 335 P2d 995.

PRACTICE TIP: Because the buyer will be deemed to know of matters within his or her diligent attention and observation, it is always advisable that the buyer personally inspect the property in addition to the inspections required of the agents in the transaction, even though CC §2079.5 does not impose an affirmative duty on a buyer to inspect or investigate facts material to the contemplated purchase. Moreover, unless the buyer has expertise in matters such as residential construction, major building components and systems, and wood-destroying organisms, it is recommended that professional inspections be performed. See §§6.75-6.77.

© The Regents of the University of California

§6.73 B. Buyer's Duty to Investigate

The issue of the buyer's duty to investigate generally arises in defense of fraud and negligence claims brought by a buyer against the seller and agents in a transaction. Defendants usually argue that the buyer's failure to act diligently or exercise reasonable care in a transaction negates an essential element of the buyer's fraud claim (*e.g.,* reasonable or justified reliance on the alleged misrepresentation), or defeats a negligence claim to the extent that the buyer's own lack of care was the proximate cause of its damages, or that defendants' liability should be reduced to the extent of the buyer's comparative negligence.

It is a well-established general rule that a buyer is justified in relying on a seller's representation of fact without independent investigation or verification, even if the buyer had an opportunity to conduct an investigation that would have disclosed the falsity of the seller's representation. See, *e.g., Hobart v Hobart Estate Co.* (1945) 26 C2d 412, 437, 159 P2d 958; *Seeger v Odell* (1941) 18 C2d 409, 115 P2d 977 (buyer's failure to investigate matters of public record not defense to active, affirmative misrepresentation); *Storage Servs. v Oosterbaan* (1989) 214 CA3d 498, 508, 262 CR 689. See also *Manderville v PCG&S Group, Inc.* (2007) 146 CA4th 1486, 1503, 55 CR3d 59 (buyer's reliance on selling agent's intentional misrepresentation negates buyer's contractual duty to investigate).

A buyer cannot claim justified reliance, however, if, under all the circumstances, including the buyer's knowledge, experience, and intelligence, such reliance was "preposterous and irrational," or if the buyer was aware of facts that would reasonably create a suspicion that the seller's representation was false, or if the buyer discovers the falsity of a material representation. *Hobart,* 26 C2d at 442; *Hartong v Partake, Inc.* (1968) 266 CA2d 942, 965, 72 CR 722; *Tarrant v Butler* (1960) 180 CA2d 235, 239, 4 CR 230; *Carpenter v Hamilton* (1936) 18 CA2d 69, 75, 62 P2d 1397. Under such circumstances, the buyer has a duty to further investigate the facts. For the definition of constructive notice, see CC §19.

A duty to investigate also arises once a seller discloses an essential fact to the buyer, after which additional details about the disclosed matter will be deemed to be within the buyer's own diligent attention. *Stevenson v Baum* (1998) 65 CA4th 159, 166, 75 CR2d 904 (statement in purchase agreement that title is subject to easements of record created duty for buyer to inspect public records to learn details about easements); *Pagano v Krohn* (1997) 60 CA4th 1, 10, 70 CR2d 1 (once seller disclosed existence of water intrusion and related litigation against developer, buyer had a duty to investigate contents of the lawsuit). When the buyer actually conducts an inspection of the property, the buyer will be presumed to know all information that would be disclosed by an inspection conducted with ordinary diligence. *Gifford v Roberts* (1947) 81 CA2d 712, 718, 184 P2d 942.

PRACTICE TIP: If a buyer chooses to rely on seller representations without independent investigation, a subsequent fraud claim by the buyer is unlikely to succeed if the matter involved is found to have been obvious and patent such that it would have been discovered in the course of a reasonably diligent inspection, or if the buyer failed to investigate the relevant details of an essential fact disclosed by the seller.

© The Regents of the University of California

§6.74 C. Scope of Buyer's Due Diligence

In every real estate transaction, the buyer must determine the appropriate scope of due diligence. This will depend, among other things, on the type and condition of the property, its intended use, its location, and the extent and quality of the seller's disclosures, as well as the buyer's knowledge, experience, and particular issues of concern. A competent real estate attorney, considering these factors, can assist the buyer in designing an appropriate scope of due diligence for the transaction.

The California Residential Purchase Agreement and Joint Escrow Instructions (see §6.24) gives the buyer the right, but not the obligation, to investigate the condition and suitability of the property to be purchased, all aspects of the property, and all matters affecting its value or desirability. See *Manderville v PCG&S Group, Inc.* (2007) 146 CA4th 1486, 1503, 55 CR3d 59. CAR's Buyer's Inspection Advisory (Form BIA), which is typically incorporated into the purchase contract (see §6.25), is useful for this task, as is the more detailed Statewide Buyer and Seller Advisory (Form SBSA), which is also widely used (see §6.27).

In most transactions, the buyer's due diligence with respect to the physical condition of the property will include the buyer's review of seller disclosures, agents' written disclosures of defects observed during their visual inspections of accessible areas of the property, a wood-destroying organism (pest) inspection and report, a home inspection and report, and the buyer's own property inspection. During inspections, the buyer, agents, and professionals should also be alert to property conditions that might suggest an unrecorded easement, such as the presence of sewage pipes, or fences, gates, and pathways, the purpose of which are not apparent. Regardless of the results of the buyer's inspections, the buyer may elect to conduct further inspections of major systems, such as roof, fireplace, septic system, as well as drainage, soil, and geologic conditions. Property inspections are discussed in §6.75.

The buyer should also investigate off-site conditions that may affect the use and enjoyment of the property, particularly if the buyer is unfamiliar with the neighborhood or has particular concerns. This off-site investigation may include the identity of the owners or occupants of adjacent properties and any unresolved neighbor disputes, the proximity of any registered sex offenders, neighborhood crime statistics, noise, unusual odors, and other nuisances.

In addition, the buyer should investigate matters of record that affect title to the property, such as recorded easements. See §§6.78-6.81. The buyer should obtain and review full copies of all documents recorded against the property.

If the property is a common interest development (CID), the buyer should carefully review, with the assistance of competent counsel, the extensive CID Disclosures, including the subdivision's governing documents, operating rules, and financial information. See §§6.60-6.63. Some of the more important matters to consider include whether the development has age or rental restrictions; the allocation of responsibility, as between owners and the homeowners' association, for maintenance, repair, and replacement of the separate interests, common area, and exclusive-use common areas; the association's insurance coverage (including property, liability, and earthquake coverage, if any), deductibles, and policy limits; and architectural controls and the procedure for obtaining approval of proposed modifications.

The buyer should also investigate governmental regulations that may affect the use of the property, such as zoning, permit requirements, development policies and restrictions, and future proposed, planned, or approved development nearby. If the property is a rental, the practitioner must research and advise the client on any applicable rent control ordinances or eviction controls and their effect on the client's ability to adjust existing rents, evict existing tenants, or freely rent the property in the future.

A buyer with children should contact local school districts regarding school assignment policies and practices. The buyer should also confirm the insurability of the property with a local insurance agent.

© The Regents of the University of California

§6.75 D. Property Inspections

In most residential transactions, a wood-destroying pest or organism inspection ("pest inspection") and a home inspection are typically performed, followed by any additional inspections that may be recommended or desired based on the condition of the property and the buyer's particular concerns. These inspections cover different matters and are regulated by different statutes.

© The Regents of the University of California

§6.76 1. Pest Inspection

Pest inspections are regulated by Bus & P C §§8500-8697.5. Pest inspectors, referred to in the statute as "field representatives," must be duly licensed by the Structural Pest Control Board and employed by a registered pest control company. Bus & P C §§8506.1, 8507. The address of every property inspected must be reported to the Board on a prescribed form no later than 10 business days after the inspection. Bus & P C §8516(b). The inspector must deliver to the person requesting the inspection, within the same time period, a report of the inspection on an approved form, meeting detailed statutory requirements. Bus & P C §8516.5. The report, among other things, must identify areas of the property that were inaccessible or otherwise not inspected and include recommendations for corrective measures. Bus & P C §8516(b)(9)-(10). These recommendations are separated into "Section 1" work for infestation or infection that is evident, and "Section 2" work for conditions that are deemed likely to lead to infestation or infection, and must include cost estimates for each such item (if cost estimates are requested and the pest company performs corrective work). Bus & P C §8516(c)(1)-(2). The inspection company must retain the original report and field notes for 3 years and must make reports available to the Board for inspection and copying or submit a copy to the Board upon request. Bus & P C §8516(i).

There is no statutory requirement that conditions identified in a pest report be corrected. If the party responsible for correction of pest work in the transaction chooses not to have the corrective work performed, the pest inspector and pest control company will not be liable for any resulting damages. However, they may be liable if found to have been negligent in the performance of the inspection. Bus & P C §8516(d). The buyer and seller may, as a matter of contract, allocate responsibility between them for correcting all or a portion of the pest work. See the California Residential Purchase Agreement and Joint Escrow Instructions, ¶4.A, in §6.24. Separately, the buyer's lender, if it has requested and reviewed the pest inspection report, may require completion of some or all of the pest work as a condition to funding the buyer's loan.

When corrective work is performed, the pest control company must complete, on a form specified by the Board, a notice of work completed and not completed, and deliver the form to the property owner and file it with the Board within 10 working days after completing the work. Originals must be retained by the pest company for 3 years, made available to the Board to review and copy, or submitted to the Board within 2 business days of a request. Bus & P C §8518. A reinspection may be performed to inspect corrective work that has been completed and must be reported on a specified form. After 4 months, however, another original inspection is required. Bus & P C §8516(b)(13). When the pest inspection has disclosed no infestation or infection, or after all corrective work has been performed and reinspected, the pest company must, on request, execute a certification that the property is free of "evidence of active infestation or infection" in visible and accessible areas. Bus & P C §8519. This certification may be given even if Section 2 work has been identified in the pest report. Bus & P C §8516(e). For information about obtaining copies of inspection reports from the Structural Pest Control Board, see the Directory.

PRACTICE TIP: The cost to correct pest infestation or infection can be material to a transaction. Therefore, it is generally advisable for a seller to have a pest inspection before marketing the property for sale. This eliminates surprises during the buyer's inspection period and allows the parties to account for the pest work in the purchase price or other transaction terms. In a "seller's market," with multiple offers on properties, a pest inspection report is typically given to potential bidders to review with the implicit understanding that a successful bidder will assume responsibility for the pest work. In a "buyer's market," the buyer will often require the seller to agree, in the purchase agreement, before a pest inspection has even been performed, to correct all Section 1 conditions and obtain a pest certification or "clearance," and even to correct Section 2 conditions. It is not advisable for sellers to assume contractual responsibility to perform Section 1 (or Section 2) work until *after* a pest inspection has been performed, because this exposes the seller to a potentially substantial, unknown liability. One alternative is for the parties to address all issues involving the physical condition of the property (including those revealed during the home inspection) at one time in conjunction with the buyer's removal of its inspection contingency. See §§6.20-6.22.

© The Regents of the University of California

§6.77 2. Home Inspection

Home inspections are regulated by Bus & P C §§7195-7199. A "home inspection" is a noninvasive physical examination, performed for a fee in connection with the transfer of real property, of the essential systems, components, or structure of a residential dwelling of one to four units, which is designed to identify material defects. Bus & P C §7195(a)(1). A "material defect" is defined as a condition that significantly affects the value, desirability, habitability, or safety of the dwelling, without reference to style or aesthetics. Bus & P C §7195(b). A home inspection also includes any consultation regarding the property that is represented to be a home inspection "or any confusingly similar term." Bus & P C §7195(a)(1). A home inspection may also include, if requested by the client, an inspection of the energy efficiency of the property. Bus & P C §7195(a)(2). See also Pub Res C §25401.7 (home inspector to provide contact information for governmental and private entities that provide home energy information).

A home inspector is any person who performs a home inspection. Bus & P C §7195(c). A home inspector who is not a licensed general contractor, structural pest control operator, architect, or registered professional engineer must perform a home inspection with the degree of care that a reasonably prudent home inspector would exercise. Bus & P C §7196. That standard is established by the standards of practice and code of ethics of the California Real Estate Inspection Association, the American Society of Home Inspectors, or other nationally recognized professional home inspection associations. Stats 1996, ch 338, §1.

A home inspection report is a written report prepared for a fee that is issued after the home inspection and clearly describes and identifies the inspected systems, structures, or components of the dwelling, and any material defects identified, and makes recommendations regarding conditions observed that may warrant further investigation or evaluation by other appropriate persons. Bus & P C §7195(c). Thus, the home inspection often functions much like an examination by a medical general practitioner, who makes appropriate referrals to specialists depending on the conditions observed during the exam. Based on the home inspector's recommendations or particular concerns of the buyer, additional inspections are often made of the roof, fireplace and chimney, swimming pool, foundation, and site drainage, and samples may be taken of suspected asbestos-containing materials and lead paint.

Any contractual provision purporting to waive the statutory duty of care for a home inspection or limiting the liability of the inspector to the fee for the inspection is contrary to public policy and invalid. Bus & P C §7198. The limitations period for an inspector's breach of the duty of care is 4 years from the date of the inspection. Bus & P C §7199.

Under the home inspector statute (Bus & P C §7197(a)), it is an unfair business practice for an inspector or inspection company, or an affiliated company, to do any of the following:

- Offer to perform for a fee any repair to a structure for which they performed an inspection within the past 12 months;
- Inspect any property in which they have an interest;
- Pay brokers or agents for referrals; or
- Accept an engagement or a fee that is contingent on the conclusions of the report, preestablished findings, or the close of escrow.

The above prohibitions do not prevent a structural pest control operator from performing repairs as a result of a structural pest control inspection. Bus & P C §7197(b).

PRACTICE TIP: The quality of home inspectors and their work product varies widely depending on the inspector's background, education and experience, and familiarity with the type of construction in the locality, among other things. The client should investigate the inspector's qualifications and membership in professional associations and the standard to be applied to the inspection. The client should also request evidence of errors and omissions coverage. Counsel should review the home inspection company's form contract for questionable provisions, including efforts to limit the inspector's liability or a requirement that the client indemnify the inspector from and against third party claims.

© The Regents of the University of California

§6.78 V. TITLE AND VESTING

Buyers' decisions regarding title issues go to the heart of every real estate transaction but often are given only passing consideration in residential transactions. The three main areas that require attention are:

- The condition of title, including all recorded and unrecorded matters affecting title (see §§6.79-6.81);
- Selection of an appropriate scope of title insurance coverage (see §§6.82-6.85); and
- Vesting of title (see §§6.86-6.92).

Decisions on these issues establish the precise real property interests being purchased, the persons and entities that are acquiring such interests and, if more than one, their respective interests and rights to convey and devise their interests, and insurance protection against challenges to such rights.

© The Regents of the University of California

§6.79 A. Condition of Title

A buyer of real estate is entitled to receive "marketable title" to the property being acquired. *King v Stanley* (1948) 32 C2d 584, 197 P2d 321. On marketability of title, see §§4.50-4.51 and California Title Insurance Practice §§6.24-6.26 (2d ed Cal CEB 1997). Ultimately, the buyer will be required to accept title subject to both recorded and unrecorded matters, except for monetary liens that the buyer is not assuming and other matters affecting title that the seller has agreed in writing to remove. See the CAR California Residential Purchase Agreement and Joint Escrow Instructions, ¶12.B, in §6.24. Therefore, in every residential transaction, the buyer must have an opportunity to review and approve title, with the assistance of a competent professional.

© The Regents of the University of California

§6.80 1. Recorded Interests in the Property

In every transaction, a Preliminary Report should be ordered from the title company the parties have selected to issue a policy of title insurance at closing. The Preliminary Report discloses, as of a specified date:

- The estate or interest in land being conveyed (*e.g.,* fee, condominium in fee);
- The legal description of the land;
- The identity of the person in whom title to the estate or interest is vested;
- Liens, encumbrances, and other matters recorded against the land, which will be excepted and excluded from coverage; and
- Various informational notes regarding the form of title insurance contemplated, recent conveyances of the subject estate or interest, and other relevant matters.

If the property is a separate interest in a common interest development, the preliminary report will also:

- Identify the type of interest being conveyed (condominium, planned development, stock cooperative);
- Describe the separate unit or lot (generally by reference to a condominium map);
- Specify any exclusive-use common areas appurtenant to the unit or lot (*e.g.,* deck, storage area, parking space) and the allocated percentage interest in the common area; and
- Identify the recorded declaration of conditions governing the development.

The Preliminary Report should be updated through the closing date to capture any newly recorded interests. For a more detailed discussion of the Preliminary Report, see California Title Insurance Practice §5.29 (2d ed Cal CEB 1997).

The Preliminary Report is not a representation as to the condition of title, but rather is an offer, in consideration for payment of a specified premium, to issue a specified title insurance product insuring against loss resulting from defects, liens, and encumbrances that are not shown as exceptions and exclusions in the Preliminary Report and are not otherwise excluded in the policy's pre-printed language attached to the Preliminary Report. *Lawrence v Chicago Title Ins. Co.* (1987) 192 CA3d 70, 74, 237 CR 264; Ins C §§12340.11, 12414.30(b).

The buyer's approval of the condition of title should be a contingency of every residential transaction. The only time this rule would not apply is when the buyer has received a Preliminary Report from an acceptable title insurer and has evaluated the title, with professional advice, before submitting a purchase offer. The CAR California Residential Purchase Agreement and Joint Escrow Instructions, ¶12.A (see §6.24) makes the buyer's approval of title a contingency of the transaction.

The scope of a buyer's review and evaluation of the Preliminary Report will depend on the nature of the property and the liens and encumbrances affecting it, as well as the buyer's intended use or other personal concerns. On reviewing preliminary reports, see California Title Insurance Practice §§2.5-2.11 (2d ed Cal CEB 1997). On preliminary reports generally, see Title Ins, chap 5. A buyer who intends to make improvements to the property should consider having an architect, engineer, or contractor review the report for locations of easements, setbacks, and the like (in addition to investigating local land use requirements applicable to the property). See §6.74.

At a minimum, in every transaction the buyer's title review should include the following:

- *Confirm the vesting of title*. Often title to residential property is held by a revocable trust (for estate planning purposes) but the seller is identified as the person who is the trustor. In that case, the trust documents should be reviewed by the title company to confirm that the seller-trustor or any successor trustee has the legal capacity to convey the property. Alternatively, as is more customary, the title company should obtain from the seller a Certification of Trust pursuant to Prob C §18100.5. See Drafting California Revocable Trusts §22.1 (4th ed Cal CEB 2003). If title is vested in a married person as his or her separate property, a quitclaim deed from the other spouse is advisable.
- *Review the legal description of the property*. The extent to which this review is conducted depends on the type of property involved. For example, a metes-and-bounds description usually is not verified unless boundaries or easement locations are material to the particular buyer. When property is described by reference to a parcel map, the map should be reviewed. Maps often depict the location of easements or disclose other matters affecting title. For common interest developments, the separate interest being purchased is typically described by reference to a recorded map that depicts the "unit" or "lot" and depicts any exclusive-use common areas (deck, storage area, parking space) appurtenant to the separate interest, to which an exclusive easement is granted.

For a thorough discussion of property descriptions, see chap 11.

- *Review easements and liens*. Review documentation of all easements and liens that will survive closing and will be excepted and excluded from title insurance. This crucial task is often overlooked. The buyer should obtain from the title company the underlying documentation of every lien on the property, except for monetary liens that are to be paid off at closing (*e.g.,* the seller's loan, unless it is being assumed by the buyer). The identification of recorded documents in the Preliminary Report is intended to put the buyer on notice. The buyer must then obtain the document to ascertain its terms. For example, if the property is subject to an easement, the buyer should review the easement agreement, which may contain payment terms and other rights and obligations that run with the land.

After the buyer completes the title review and before the agreed contingency period expires, the buyer should provide the seller, in writing, with a list of any matters affecting title that are disapproved and require the seller to agree to remove such matters before, and as a condition of, closing. Supplemental escrow instructions, typically prepared by the escrow company, should reference the title exceptions that will survive escrow. These instructions should be reviewed carefully to make sure that no matters disapproved by the buyer have been included. On escrow instructions, see §§15.31-15.74.

© The Regents of the University of California

§6.81 2. Unrecorded Interests in the Property

The seller has a duty to disclose to the buyer all known matters affecting title, whether or not recorded. See §§6.36-6.37. Nevertheless, the buyer should be advised, as part of its property inspection, to look for any evidence of undisclosed interests (*e.g.,* easements), particularly if the buyer intends to develop or use the property in a manner different from its existing use. If unrecorded interests affecting the use and development of the land are a concern, the buyer should attempt to secure a title insurance endorsement covering such matters. See California Title Insurance Practice, chap 6 (2d ed Cal CEB 1997).

© The Regents of the University of California

§6.82 B. Residential Title Insurance Policies

The most commonly used forms of title insurance in California are published by the California Land Title Association (CLTA) and the American Land Title Association (ALTA). Both CLTA and ALTA offer separate policy forms for owners and lenders. In residential transactions in California involving one to four residential units, it is now most common to use the CLTA Homeowner's Policy in conjunction with the ALTA Loan Policy. ALTA's Homeowner's Policy is also used, although its coverage is generally not as broad as the CLTA Homeowner's Policy. Both the CLTA and ALTA policies are written in "plain language" and only insure "natural persons," which is defined to include trustees, including institutional trustees. The CAR California Residential Purchase Agreement and Joint Escrow Instructions, ¶12.E (see §6.24) provides that the buyer will receive the CLTA/ALTA Homeowner's Policy. For a copy of the CLTA/ALTA Homeowner's Policy form, see California Title Insurance Practice, App O (2d ed Cal CEB 1997). For a detailed discussion of residential title insurance policies, see Title Ins §§7.36-7.49.

The following sections generally discuss key provisions of the CLTA Homeowner's Policy with reference to differences in coverage under the ALTA Homeowner's Policy. Because the scope of coverage and application of exclusions is often complex, the following discussion is necessarily a summary intended to familiarize the practitioner with the issues. An attorney representing a residential buyer should review specific policy language, as well as available endorsements, to make sure that the broadest coverage is obtained.

© The Regents of the University of California

§6.83 1. Coverage Statement

The Coverage Statement in the CLTA/ALTA Homeowner's Policy provides that the title insurer will insure against actual loss from 29 enumerated "Covered Risks" that existed on the policy date. See California Title Insurance Practice §7.39 (2d ed Cal CEB 1997) for a list of covered risks. Deductibles and policy limits apply to certain of the risks. The policy also insures against loss from covered risks that materialize after the policy date, including:

- Various claims of superior title, title defects, or rights to use the property, including easements;
- Liens for labor and materials furnished before the policy date;
- Damage to improvements because of the future exercise of a right to use the surface;
- A third party's attempt to enforce a discriminatory covenant, condition, or restriction;
- Supplemental real estate taxes assessed because of construction or change in ownership or use that occurred before the policy date; and
- An encroaching structure built by a neighbor (other than a boundary wall or fence).

The insurer assumes a duty to defend the insured in any legal action, but only with respect to the part of the action that is based on a covered risk not excepted or excluded from coverage in the policy. The insurer has the right to end its duty to defend by taking various actions, including paying or settling the claim.

© The Regents of the University of California

§6.84 2. Exceptions and Exclusions

The title policy will state exceptions to title, which are the recorded liens and encumbrances identified in the Preliminary Report. In addition to those exceptions, the policy includes various exclusions from coverage. The CLTA Homeowner's Policy excludes the following:

- With certain exceptions, the exercise of governmental police power or the existence or violation of an ordinance, law, or regulation concerning building, zoning, land use, improvements on land, land division, and environmental protection, unless notice of the violation or enforcement of such matters appears in the public records at the policy date;
- The failure of existing structures on the property to comply with applicable building codes, unless notice of such violation appears in the public records at the policy date;
- The right to take the land by condemnation unless notice of the exercise of the right appears in the public records at the policy date or the taking occurred before the policy date without the insured's knowledge and is binding on the insured;
- Risks that are created, allowed, or agreed to by the insured; that are known to the insured, but not the insurer, at the policy date (unless a matter of public record); that result in no loss to the insured; or that occur after the policy date (except for those post-policy-date risks expressly covered);
- The failure to pay value for the title to the property; and
- With certain exceptions, lack of a right to land outside of the property described in the policy and in streets, alleys, or waterways that touch the land.

© The Regents of the University of California

§6.85 3. Endorsements

Both CLTA and ALTA have prepared standard form endorsements (more than 150 CLTA endorsements and nearly 50 ALTA endorsements) for use with their policies. Some of these apply to residential transactions and may be available for payment of an additional premium, but availability varies by title insurer. Whether an endorsement is desirable in a particular transaction should be evaluated by an attorney who has knowledge of the property and the circumstances of the transaction, and can evaluate the potential title defects or claims that may exist or arise, in consultation with a knowledgeable title officer. Certain endorsements will require a chain-of-title search by the insurer and physical inspection of the property. In the extremely rare situation when the title policy and available endorsements do not address the needs of the insured, the insured may be able to negotiate a special endorsement with the title insurer to cover the unique circumstance. For a list of available endorsements see California Title Insurance Practice, App I (2d ed Cal CEB 1997).

Standard form endorsements exist that extend coverage to such matters as:

- Verification that an access easement described in the title policy provides access to a named public street and has not been extinguished by adverse possession, encroachment, or other unrecorded matters;
- Encroachments onto adjoining land or an easement;
- Violations of recorded covenants, conditions, and restrictions or judicial enforcement of such violations;
- Mechanics' liens;
- The boundaries of common area in a common interest development; and
- Judgments requiring the removal of a residential structure or cessation of its use for residential purposes based on a zoning ordinance violation that existed on the policy date.

© The Regents of the University of California

§6.86 C. Vesting of Title

Co-owners of property have several options for taking and holding title to property. Before 2001, the primary forms of co-ownership in California were (1) joint tenancy, (2) tenancy in common, (3) community property (for married spouses only), and (4) tenancy in partnership. CC §682. In 2001, California added a new form of property ownership, community property *with right of survivorship* (CC §682.1), and in 2003 extended the same rights of property ownership enjoyed by married persons to registered domestic partners, retroactive to 2000 (Rev & T C §62) (Fam C §297.5). The salient characteristics of each of these forms of co-ownership are outlined below. The form of co-ownership that is most appropriate for a particular client's situation should be determined by knowledgeable real estate, estate planning, and tax attorneys after careful consideration of the financial arrangement between the co-owners, their marital or domestic-partnership status, their investment objectives, estate plans, and the tax implications of each form of ownership. In addition, other forms of ownership, such as use of a revocable trust, should be considered.

© The Regents of the University of California

§6.87 1. Joint Tenancy

A "joint interest" or joint tenancy is an interest in property owned by two or more persons in equal shares. CC §683. Each joint tenant concurrently owns an undivided equal share of the entire property. *Rupp v Kahn* (1966) 246 CA2d 188, 196, 55 CR 108. When one joint tenant dies, by operation of law the surviving joint tenant owns the entire property. *Grothe v Cortlandt Corp.* (1992) 11 CA4th 1313, 1317, 15 CR2d 38. Thus, a joint tenancy interest cannot be disposed of by will. This "right of survivorship" was, for centuries, unique to joint tenancy until the new "community property with right of survivorship" was created in 2001. See §6.91. A joint tenancy may be terminated by one of several actions, including the unilateral conveyance by one joint tenant to a third person, recordation of a written declaration, agreement of the joint tenants, a partition decree, or judgment. When the joint tenancy is severed, it becomes a tenancy in common and the right of survivorship terminates. *Estate of Propst* (1990) 50 C3d 448, 455, 268 CR 114. Thereafter, each tenant in common may make a testamentary disposition of his or her interest in the property. *Estate of Grigsby* (1982) 134 CA3d 611, 618, 184 CR 886. For a discussion of language to use in a deed creating a joint tenancy, see §10.31.

© The Regents of the University of California

§6.88 2. Tenancy in Common

A tenancy in common is any interest owned in common by two or more persons that is not a joint tenancy, tenancy in partnership, or community property. CC §§685-686. Each tenant in common has an equal right of possession and cannot exclude the other(s) from any part of the property, unless the co-tenants agree otherwise. *Estate of Horn* (1951) 102 CA2d 635, 640, 228 P2d 99. Unlike a joint tenancy, however, tenancy-in-common interests need not be equal, and there is no right of survivorship. *Estate of England* (1991) 233 CA3d 1, 4, 284 CR 361. Therefore, co-owners can conform their ownership interests to their respective contributions to the cost of purchasing and owning a property, and each can make a testamentary disposition of his or her interest. For a discussion of language to use in a deed creating a tenancy in common, see §10.32.

© The Regents of the University of California

§6.89 3. Community Property

A husband and wife can hold property as a joint tenancy, a tenancy in common, community property, or community property with right of survivorship. Fam C §750. Community property is defined as property acquired by a married person during marriage while domiciled in California. CC §687; Fam C §760. California law requires marriage to be between a man and a woman. Fam C §§308, 308.5. Community property rights have also been extended to a "putative spouse," who believes in good faith, but incorrectly, that the parties are married (*Patillo v Norris* (1976) 65 CA3d 209, 217, 135 CR 210), but not to knowingly unmarried, cohabitating parties (*Marvin v Marvin* (1976) 18 C3d 660, 681, 134 CR 815).

California community property law involves a complex body of rules and principles beyond the scope of this chapter; the discussion here addresses only whether a husband and wife, who will purchase the property using only assets acquired during their marriage, should take title as community property or otherwise. With community property, as with a joint tenancy, a husband and wife have equal interests during their marriage. Fam C §751. Unlike joint tenancy, however, spouses with community property interests have the flexibility, both before and during marriage, to specify their property interests in writing, alter or transmute those interests, and compromise their interests in dissolution of marriage. See Fam C §§850-853, 1500, 2550. Also unlike joint tenancy, there is no right of survivorship attendant to community property unless specified in the conveyance document. Nevertheless, if a spouse dies without a will, the community property interest of the deceased spouse passes to the survivor. Prob C §6401. A spouse may, of course, dispose of his or her one-half community interest by will. Prob C §§100-101, 6101.

For a discussion of language to use in a deed creating a community property interest, see §10.33. For a discussion of language to use in changing title from joint tenancy to community property, see §10.33.

© The Regents of the University of California

§6.90 4. Registered Domestic Partners

In 2003, the California legislature enacted the California Domestic Partner Rights and Responsibilities Act of 2003 (Stats 2003, ch 421), which extends the rights and responsibilities of marriage to registered domestic partners. Fam C §297.5. "Domestic partners" are defined as two adults "who have chosen to share one another's lives in an intimate and committed relationship of mutual caring." Fam C §297(a). A domestic partnership is established when both persons file a Declaration of Domestic Partnership with the Secretary of State as specified in the Act and, at the time of filing, they have a common residence, are not married or in another domestic partnership, not related by blood in a way that would prevent them from marrying, are both at least 18 years old, and are either of the same sex or of the opposite sex if one of the partners is over the age of 62 and meets certain Social Security eligibility requirements. Fam C §297(b).

The Act provides, among other things, that registered domestic partners shall have "the same rights, protections, and benefits, and shall be subject to the same responsibilities, obligations, and duties" as are granted to or imposed on spouses, or on a widow or widower. Fam C §297.5(a), (c). Revenue and Taxation Code §62 affirms this right as of 2000.

© The Regents of the University of California

§6.91 5. Community Property With Right of Survivorship

In 2001, the California legislature created a new form of property ownership, community property with right of survivorship, which combines the attributes of community property and joint tenancy ownership. CC §682.1(a). By virtue of the California Registered Domestic Partner Rights and Responsibilities Act of 2003, this new form of co-ownership is available to duly registered domestic partners. See §6.90. For the parties to effectively take title as community property with right of survivorship, the transfer document must include an express declaration that the property is community property with right of survivorship, which may be accepted in writing on the face of the document by a statement signed or initialed by the grantees. While still alive, the spouses or registered domestic partners may terminate the right of survivorship by the same procedures used to terminate a joint tenancy. CC §682.1(a). See §6.87. On the death of one of the spouses or registered domestic partners, the property passes to the survivor, without administration, in the same manner as joint tenancy property.

PRACTICE TIP: Under this new form of ownership, a surviving spouse or surviving registered domestic partner is able to avoid the cost and delay of probate (as with joint tenancy); however, only a surviving spouse can realize the federal tax benefit of a step-up in the tax basis of the entire property because federal law does not recognize same-sex marriage or its equivalent. The new form of ownership would not be appropriate if one or both spouses or registered domestic partners wishes to devise his or her property interest to a third party, typically a child from a previous relationship. In such case, community property without the right of survivorship (if the couple is married) or a trust should be considered.

© The Regents of the University of California

§6.92 6. Tenancy in Partnership

Tenancy in partnership is not a common form of ownership of residential property. A "partnership interest" in property is defined as one owned by several persons in partnership, for partnership purposes. CC §684. Partnership property is not co-owned by the individual partners, as in the other forms of co-ownership (see §§6.87-6.91). Rather, the property is owned by the partnership, which is an entity distinct from the individual partners, formed to conduct a business for profit. Corp C §§16201, 16202(a), 16203. Thus, the individual partners have no legal right in the partnership property that can be transferred. Corp C §16501. Rather, their rights are limited to sharing in the profits and losses of the partnership and the right to receive distributions. Corp C §16502. Furthermore, a partner cannot devise partnership property. Rather, upon death the partner is "dissociated" from the partnership, and the partnership must purchase his or her interest. Corp C §§16601(7)(A), 16701(a).

© The Regents of the University of California

§6.93 VI. TAX CONSIDERATIONS

The purchase and sale of residential real property is subject to taxation on the federal, state, and local levels. Particularly in view of the significant appreciation in the market value of California real estate in recent decades, the tax consequences of a transaction are generally of primary importance to both sellers and buyers. Tax rules and regulations tend to be detailed and complex, with numerous exclusions and exemptions. Therefore, clients should usually be referred to qualified tax attorneys or accountants for advice on the tax implications of a particular transaction. Nevertheless, attorneys representing clients in residential transactions should have a basic understanding of the relevant tax laws and regulations.

This section briefly discusses the following tax issues commonly encountered in a residential transaction:

- Withholding tax (see §6.94);
- Transfer tax (see §6.95);
- Property tax (see §6.96); and
- Capital gains tax (see §6.97).

For a discussion of tax-deferred exchanges, see Real Property Exchanges (3d ed Cal CEB 2002).

© The Regents of the University of California

§6.94 A. State and Federal Withholding Taxes

State and federal laws require buyers, under certain circumstances, to withhold a portion of the sale price from the seller and forward the amount withheld to the appropriate tax authority, unless an exemption applies.

California law generally requires the buyer of a California real property interest to withhold 3-1/3 percent of the gross sale price from the seller and to transmit the withheld amount to the Franchise Tax Board unless an exemption applies. Rev & T C §18662(e)(2)(A). For further discussion regarding California withholding requirements, see §§15.75-15.79.

If the seller is a "foreign person," the Foreign Investment in Real Property Tax Act of 1980 (FIRPTA) (Pub L 96-499, 94 Stat 2682) requires a buyer to withhold 10 percent of the gross sales price from the seller and to transmit the withheld amount to the Internal Revenue Service. IRC §1445(a). For further discussion regarding FIRPTA withholding requirements, see §§15.80-15.84.

© The Regents of the University of California

§6.95 B. Transfer Tax

The Documentary Transfer Tax Act (Rev & T C §§11911-11913) authorizes counties to impose a transfer tax on the conveyance, transfer, or assignment of an interest in real property at the rate of 55 cents per $500 in value transferred. Rev & T C §11911(a). If a county has imposed a transfer tax, any city within that county may impose a transfer tax of one-half of the amount of the county tax, which is credited against the county tax. Rev & T C §11911(b)-(c). In addition, charter cities may impose by ordinance an additional transfer tax that exceeds the statutory limits. See Cal Const art XI, §5; *Fisher v County of Alameda* (1993) 20 CA4th 120, 124, 24 CR2d 384 (city is empowered to impose real estate transfer tax, taking precedence over conflicting provisions of state law by virtue of home-rule powers conferred on charter cities by Cal Const art XI, §5).

Statutory exemptions from the transfer tax include:

- Written instruments given to secure a debt (Rev & T C §11921);
- Certain transfers by inter vivos gift or inheritance (Rev & T C §11930);
- Certain transfers in lieu of foreclosure (Rev & T C §11926);
- Certain interspousal transfers (Rev & T C §11927);
- Transfers of certain partnership interests (Rev & T C §11925); and
- Transfers made to effect a reorganization plan in bankruptcy or receivership proceedings, or whereby a mere change in identity, form, or place of organization is effected (Rev & T C §11923).

Additional exemptions may be found in each county or city ordinance that authorizes the transfer tax.

PRACTICE TIP: Several California charter cities impose steep transfer taxes in addition to the county transfer tax. For example, the City of Berkeley and City of Oakland each impose a transfer tax of $15 per $1000 of value. See Berkeley Muni C §7.52.040; Oakland Muni C §4.20.020. These taxes can significantly increase the buyer's cost to purchase a property and decrease the seller's profit from a sale. Practitioners should determine whether the city in which the subject property is located imposes a transfer tax, and evaluate potentially applicable exemptions in the statute as well as county and city ordinances. Although allocation of transfer taxes between seller and buyer is negotiable, the Documentary Transfer Tax Act requires the seller to pay the county (and statutory city) transfer tax. Rev & T C §11912. Any city transfer tax is typically allocated between seller and buyer based on local custom (often split 50/50).

© The Regents of the University of California

§6.96 C. Property Tax

Proposition 13 was adopted by California voters in 1978 with the stated goal of providing real property tax relief. Under Proposition 13, when there is a change in ownership of California real property, the property is reassessed at its current fair market value (typically, the sale price) and the new owner's property tax is calculated based on the reassessed value. Rev & T C §50. Many common transfers, however, are deemed not to involve a change in ownership that would trigger a reassessment. These include:

- Certain transfers that change the method of holding title but not the proportional interests held (Rev & T C §62(a));
- Transfers into a revocable trust (Rev & T C §62(d));
- Interspousal transfers (Rev & T C §63);
- Transfers between ex-spouses under a property settlement agreement or decree of dissolution or legal separation (Rev & T C §63(c));
- Transfers between registered domestic partners (commencing on January 1, 2000, with a right to apply for reversal of any reassessment made between January 1, 2000, and January 1, 2006, in contravention of the exemption) (Rev & T C §62(p); see Fam C §297);
- Transfers between parents and children of the principal residence or up to $1 million of "full cash value" of all other real property (Rev & T C §63.1(a)); and
- Transfers from grandparents to grandchildren, only if the grandchild's parents are deceased (Rev & T C §63.1(a)(3)).

For a detailed chart listing transfers that do and do not trigger a reassessment, see App A.

In certain circumstances, a taxpayer who is age 55 or older, or is severely and permanently disabled, may transfer the base-year value of his or her principal residence (*i.e.,* its original assessed value under Proposition 13 plus permitted inflation adjustments) to a replacement principal residence of equal or lesser value. See Rev & T C §69.5(a)(1)-(2), (g)(2). See Rev & T C §69.5(g)(5) (defining "equal or lesser value"), 69.5(g)(12) (defining "severely and permanently disabled"). This transfer right applies only if the replacement dwelling is located in the same county as the original property or in another county in which the board of supervisors has adopted an ordinance permitting an intercounty transfer of base-year value. Rev & T C §69.5(a). The transfer right may only be exercised once, except that a taxpayer who exercises the right based on his or her age may do so again if he or she thereafter becomes severely and permanently disabled. Rev & T C §69.5(b)(7). A claim for exemption from reassessment must be filed within 3 years of the date the replacement dwelling was purchased or construction of a replacement dwelling was completed. Rev & T C §69.5(f).

Similarly, the base-year value of a property substantially damaged or destroyed by a qualified disaster may be transferred to a comparable replacement property (*i.e.,* similar in size, utility, and function) that is newly acquired or constructed within 3 years after the disaster. See Rev & T C §69.

Finally, certain types of construction are exempt from reassessment, including construction to make a dwelling more accessible to a severely and permanently disabled person who resides in the dwelling, and certain seismic retrofitting work. See Rev & T C §§74.3, 74.5.

© The Regents of the University of California

§6.97 D. Capital Gains Tax

An individual's principal residence is a capital asset. IRC §1221. Gain on its sale will therefore be taxed as long-term or short-term capital gain, depending on the taxpayer's holding period. Since enactment of the Taxpayer Relief Act of 1997 (Pub L 105-34, 111 Stat 788), sellers who have owned and used a home as their personal residence for at least 2 of the 5 years before the sale can exclude at least some of the gain on the sale from income. IRC §121(a). There are a few limited exemptions from the 2-year requirement that apply if the primary reason for the sale or exchange is a change in place of employment, health, or unforeseen circumstances, in which case the amount of the exclusion is prorated. See Treas Reg §1.121-3. The exclusion applies to individuals as well as to grantors of revocable trusts. IRC §676.

The exclusion is subject to several important limitations:

First, the exclusion can be used only once every 2 years. IRC §121(b)(3).

Second, single persons can exclude up to a maximum of $250,000. IRC §121(b)(1).

Third, joint filers can exclude up to $500,000 if either spouse has owned the home for at least 2 of the 5 years before the sale; both spouses must have used the home as their principal residence for at least 2 of the 5 years before the sale; and neither spouse is ineligible for the exclusion because of the once-every-2-year limitation. IRC §121(b)(2)(A). If joint filers do not meet all of these requirements, they may determine the exclusion amount on an individual basis; thus, the allowable exclusion would be equal to the sum of the individual exclusions to which each spouse would have been entitled if they had not been married. IRC §121(b)(2)(B).

Fourth, an unmarried individual whose spouse is deceased on the date of the sale may exclude up to $500,000 if the sale occurs not later than 2 years after the date of the spouse's death and the joint-filer requirements were satisfied immediately before the date of death. IRC §121(b)(4).

Fifth, the Housing and Economic Recovery Act of 2008 (Pub L 110-289, 122 Stat 2911) added an important new limitation on the exclusion, which applies to sales and exchanges that occur after December 31, 2008. IRC §121(4). (Note: This Act enacted a second subparagraph(b)(4).) New IRC §121(4) provides that when an individual converts a rental property or second home to his or her principal residence after December 31, 2008, the taxable portion of any gain on a subsequent sale will be determined by use of a fraction—the numerator of which is the amount of time beginning on January 1, 2009, that the property was used as a rental or second home, and the denominator of which is the total number of years of ownership of the property (including prior to January 1, 2009). IRC §121(4). Gains from the investment/rental use of the property will be taxed at prevailing capital gains rates, and gains from the principal residence use will be taxed subject to the exclusions applicable to the sale of a principal residence. If the gain on the sale exceeds the amount of the exclusion, the excess will be taxed at the applicable capital gains rate. A seller may not deduct losses on the sale of his or her principal residence.

EXAMPLE: Seller purchased a property on January 1, 1998, for $200,000 and owned the property for 20 years through December 31, 2017. Seller lived in the property as her principal residence for 10 years from January 1, 1998, through December 31, 2007. On January 1, 2008, Seller converted the property to a rental, and rented it for 5 years through December 31, 2012. She then moved back into the property on January 1, 2013, and sold it 5 years later on January 1, 2018, for $600,000. To determine taxable gain, the numerator would be 4 (the number of years after January 1, 2009, that the property was rented), and the denominator would be 20 (the total number of years of ownership). The Seller's gain would be $400,000 (assuming no improvements were made to the property that increased her cost basis). Twenty percent (20% or 4/20) of that gain ($400,000) is $80,000, which would be taxed at the prevailing capital gains rate at the time of the sale. Of the remaining $320,000 in gain, $250,000 would be excluded on the basis of the principal residence use, and the remaining $70,000 over the exclusion would be taxed at the prevailing capital gains rate.

© The Regents of the University of California

§6.98 VII. FAIR HOUSING AND ANTIDISCRIMINATION LAWS

Various federal, state, and local laws and ordinances prohibit discrimination against certain protected classes in the sale, leasing, and use of residential property, and provide procedures and remedies for redressing such discrimination. For other discussions of these laws, see California Landlord-Tenant Practice §§2.29-2.60 (2d ed Cal CEB 1997) and Advising California Common Interest Communities §§8.42-8.60 (Cal CEB 2003).

Housing discrimination in California is principally governed by two federal statutes and two state statutes. The federal statutes are the Civil Rights Act (42 USC §§1981, 1981a, 1983, 1988) and the Fair Housing Act (FHA) (42 USC §§3601-3631), enacted as Titles VIII and IX of the Civil Rights Act of 1968, as amended by the Fair Housing Amendments Act of 1988 (42 USC §§3601-3631). The state statutes are the Unruh Civil Rights Act (CC §51) and the Fair Employment and Housing Act (FEHA) (Govt C §§12900-12996). Although these statutes often overlap, depending on the type of discrimination alleged, they differ in terms of covered classes, exemptions, procedural rights, and remedies. Therefore, in determining which statutes apply, the practitioner must consider the type of discrimination involved, the context in which it has arisen, and the redress sought by the client. The individual Acts are discussed in more detail in §§6.99-6.102.

© The Regents of the University of California

A. Federal Law

§6.99 1. Civil Rights Act of 1866

The Civil Rights Act (42 USC §§1981, 1981a, 1983, 1988) prohibits discrimination based on race. 42 USC §1982. There are no exemptions. Private litigants who are U.S. citizens may file a claim under the Civil Rights Act in state and federal court. *Sullivan v Little Hunting Part, Inc.* (1969) 396 US 229, 24 L Ed 2d 386, 90 S Ct 400. Remedies include injunctive relief, compensatory damages including out-of-pocket expenses, mental anguish, and personal humiliation (*Phiffer v Proud Parrot Motor Hotel, Inc.* (9th Cir 1980) 648 F2d 548), and punitive damages (*Woods-Drake v Lundy* (5th Cir 1982) 667 F2d 1198). The prevailing party may also recover attorney fees and costs. 42 USC §1988(b).

© The Regents of the University of California

§6.100 2. Fair Housing Act

The Fair Housing Act (FHA) (42 USC §§3601-3631) applies more broadly than the Civil Rights Act and adds an administrative remedy, but also has several exemptions. The FHA prohibits discrimination against any person—not just U.S. citizens—in the sale or rental of a dwelling, or in related advertising and lending, based on the person's race, color, religion, sex, familial status, or national origin. 42 USC §3604.

The FHA also prohibits discrimination based on a person's "handicap" and requires landlords to make reasonable accommodations and to allow reasonable modifications to a dwelling unit for a person with a handicap. 42 USC §3604(f); 24 CFR §§100.201-100.205. "Handicap" is defined to include an actual or perceived physical or mental impairment that substantially limits one or more of a person's major life activities, but does not include illegal drug use or addiction. 42 USC §3602(h). The Unruh Act also contains a similar prohibition against physical and mental "disability" discrimination, without the FHA's "substantial limitation" requirement. See §6.101.

The FHA does not cover discrimination based on marital status, age, or sexual orientation; however, these are covered by California antidiscrimination law. See §§6.101-6.102.

The following are exempt from the FHA:

- Single-family homes for sale or rent by the owner(s), if specified conditions are met (42 USC §3603(b)(1));
- Rooms or units in a dwelling with no more than four families living independently of one another, one unit of which is owner-occupied (42 USC §3603(b)(2));
- Rentals by religious organizations and private clubs, if specified conditions are met (42 USC §3607(a));
- Housing with reasonable local, state, or federal restrictions on the maximum number of occupants (42 USC §3607(b)(1)); and
- Qualified senior housing (42 USC §3607(b)(1)-(3); see §6.103).

The FHA preempts state and local laws that provide less protection to covered classes, but expressly authorizes state laws that grant additional protections. 42 USC §3615.

There are two independent means for private enforcement of the FHA. Under the first, an aggrieved person may file an administrative complaint with the U.S. Department of Housing and Urban Development (HUD). 42 USC §3610. HUD, or the state agency to which the complaint may be referred under 42 USC §3610(f), serves the complaint on the respondent for an answer and then investigates the claim and engages in a conciliation process. 42 USC §3610(a)-(b). If no conciliation agreement results and HUD determines there is reasonable cause to believe housing discrimination has occurred, the Secretary of HUD must issue a charge under 42 USC §3612 or dismiss the complaint. 42 USC §3610(g)(3). If a charge is issued, the respondent has a right to an administrative hearing or may elect to have the charge decided in a judicial proceeding. 42 USC §§3610(h), 3612(a). The administrative law judge may issue an order with remedies including actual damages, injunctive and other equitable relief, civil penalties up to $50,000 for each separate and distinct act of discrimination, and an award of attorney fees and costs to the prevailing party. 42 USC §3612(g), (p). The order is subject to judicial review. 42 USC §3612(i).

Under the second private enforcement alternative to the FHA, an aggrieved person may commence a civil action in state or federal court without having to exhaust administrative remedies. 42 USC §3613. The filing of an administrative complaint does not bar the filing of a civil action on the same claim; however, if an administrative hearing on the claim has commenced or a conciliation agreement has been executed, a civil action may not be filed except to enforce the agreement. 42 USC §3613(a)(2)-(3). On timely application, the Attorney General may intervene in such a civil action on a finding that the case is of general public importance or initiate a civil enforcement action when, in addition, there has been a pattern and practice of discrimination. 42 USC §§3613(e), 3614. The same remedies can be obtained in a civil action as in an administrative action. 42 USC §3613(d).

© The Regents of the University of California

B. State Law

§6.101 1. Unruh Act

The Unruh Civil Rights Act (CC §51) prohibits "all business establishments of every kind whatsoever" from arbitrary discrimination based on personal characteristics, which include sex, race, color, religion, ancestry, national origin, disability, medical condition, marital status, and sexual orientation. CC §51. Age discrimination in the sale or renting of housing is also prohibited. CC §51.2.

The characteristics listed in the Unruh Act are illustrative rather than restrictive. The Act covers all arbitrary discrimination by a business establishment. *Harris v Capital Growth Investors XIV* (1991) 52 C3d 1142, 1152, 278 CR 614; see *In re Cox* (1970) 3 C3d 205, 90 CR 24 (exclusion of a man from a shopping center because of long hair and unconventional dress violated the Act). Moreover, discrimination based on the *perception* that a person has one or more of the protected characteristics or associates with a person who has, or is perceived to have, such characteristics, is also prohibited. CC §51(e)(5).

"Business establishment" is not defined in the Unruh Act, but has been broadly interpreted. See *Warfield v Peninsula Golf & Country Club* (1995) 10 C4th 594, 620, 42 CR2d 50. In the context of the purchase and sale of residential real property, the following have been found to be business establishments subject to the Act:

- Condominium homeowners' associations (*O'Connor v Village Green Owners Ass'n* (1983) 33 C3d 790, 191 CR 320);
- Subdividers (*Burks v Poppy Constr. Co.* (1962) 57 C2d 463, 468, 20 CR 609);
- Landlords (*Marina Point, Ltd. v Wolfson* (1982) 30 C3d 721, 730, 180 CR 496); and
- Mobilehome park owners (*Winchell v English* (1976) 62 CA3d 125, 129, 133 CR 20).

The Unruh Act may be enforced by private persons, as well as the California Attorney General, in a civil action in state court. Available remedies include injunctive relief (*Burks,* 57 C2d at 470), compensatory damages, statutory penalties, attorney fees, and costs. CC §52(a).

© The Regents of the University of California

§6.102 2. Fair Employment and Housing Act (FEHA)

The Fair Employment and Housing Act (FEHA) (Govt C §§12900-12996) declares that the right to seek, obtain, and hold housing without discrimination based on race, color, religion, sex, sexual orientation, marital status, national origin, ancestry, familial status, disability, or any other basis prohibited by the Unruh Act is a civil right and that such discrimination is against public policy. Govt C §12955. Like the Unruh Act, FEHA protects against the perception that a person has one of the protected characteristics or associates with a person who has or is perceived to have such characteristics. Govt C §12955(m).

In enacting FEHA, the legislature expressly intended to regulate employment and housing discrimination without limiting the application of the Unruh Act. Govt C §12993(c). Thus, FEHA provides greater protection than the FHA by prohibiting discrimination based on ancestry, disability, marital status, and sexual orientation and by providing a more restrictive exemption for senior housing. See Govt C §12955.9. See discussion of senior housing in §6.103.

Under FEHA, discrimination with respect to protected classes includes, among other things, refusal to sell and rent housing or to negotiate for its sale or rental; a false representation that housing is not available for sale or rental; any other denial or withholding of housing; provision of inferior terms, conditions, privileges, facilities or services, or harassment in connection with housing; cancellation or termination of a sale or rental agreement; and providing segregated housing accommodations. Govt C §12927(c)(1). Specific discriminatory acts that are prohibited are enumerated in Govt C §12955. See *Hall v Butte Home Health, Inc.* (1997) 60 CA4th 308, 319, 70 CR2d 246 (restrictive covenant prohibiting residential care facility for elderly disabled was unenforceable under Govt C §12955).

Discrimination under FEHA does not include refusal to rent a portion of an owner-occupied house to a boarder, provided that no more than one boarder will live in the house and as long as no discriminatory advertisement is used, nor does it include an advertisement for the sharing of living areas in a dwelling that states or implies the housing is available only to a person of one sex. Govt C §12927(c)(2). FEHA does not prohibit religious organizations from limiting the sale, rental, or occupancy of dwellings owned or operated for noncommercial purposes to persons of the same religion, unless membership in the religion is restricted on account of race, color, or national origin. Govt C §12955.4.

The procedures for enforcing FEHA and available remedies are substantially similar to the procedures and remedies under the FHA. See Govt C §§12980-12989.3 and §6.100. An aggrieved party may proceed under FEHA as well as the Unruh Act, if applicable, but if an action has been filed under the Unruh Act, proceedings under FEHA will be stayed pending resolution of that action. Govt C §12980(a).

FEHA also creates procedures for the modification of recorded covenants to remove discriminatory restrictions and makes recording of a document to add a racially restrictive covenant a misdemeanor. Govt C §§12956.1(c), 12956.2. If the discriminatory restriction is in the governing document of a common interest development, however, the owner must follow the procedure described in CC §1352.5 to remove the restriction.

© The Regents of the University of California

§6.103 C. Senior Citizen Housing

Senior citizen housing that meets certain statutory requirements is exempt from both federal and state antidiscrimination provisions. 42 USC §3607(b)(2); CC §51.3; Govt C §12955.9. These laws involve the intersection of two competing public policies: the desire to establish and preserve housing to meet the needs of senior citizens and prevention of housing discrimination against families with children under the age of 18. California's senior-housing exemption is to be construed to afford greater rights and remedies to aggrieved persons than those afforded under federal law. Govt C §12955.6.

Under the federal FHA, qualified "housing for older persons" (HOP) is exempt from the prohibition against "familial status" discrimination, which refers to discrimination against persons under age 18 living with a parent or person with legal custody or their designee, or a pregnant person, or persons seeking legal custody of a minor. 42 USC §§3607(b)(2), 3602(k). See also Govt C §12955.2 (definition of "familial status" under FEHA). HOP is defined to include housing (1) provided under certain state and federal programs to assist the elderly, or (2) intended for, and solely occupied by, persons 62 years of age or older, or (3) intended and operated for occupancy by persons 55 years of age where at least 80 percent of units are occupied by at least one person who is at least 55 years old, and the housing facility or community publishes and adheres to policies and procedures demonstrating the intent to restrict the age of residents and complies with certain rules for verification of occupancy. 42 USC §3607(b)(2).

California's FEHA exempts from the prohibition against familial-status discrimination HOP, which it defines to include housing provided under state and federal programs that meet the standards for senior housing set forth in the Unruh Act. Govt C §12955.9(a), (b)(1), (2). (FEHA also exempts mobilehome parks that meet the federal definition of HOP. Govt C §12955.9(b)(3).)

Under the Unruh Act, a "senior citizen housing development" is exempt from the Act's age discrimination prohibition except to the extent preempted by the federal FHA's prohibition against familial-status discrimination. CC §51.2(a). A "senior citizen housing development" is defined as a residential development that is developed or substantially rehabilitated or renovated for senior citizens and that has at least 35 dwelling units (only 20 dwelling units are required in Riverside County). CC §§51.3(b)(4), 51.11(b)(4), (j). In addition, senior housing must be designed to meet the physical and social needs of senior citizens. CC §51.2(d). These design requirements do not apply to housing constructed before February 8, 1982, or to housing located in Riverside County. CC §51.2(a), (c). Senior housing constructed on or after January 1, 2001, is presumed to meet applicable design requirements if certain criteria are met. See CC §§51.2(d), 51.4, 51.12.

"Senior citizen" is defined as a person age 62 or older, or a person age 55 or older in a senior citizen housing development. CC §51.3(b)(1); see *Park Redlands Covenant Control Comm. v Simon* (1986) 181 CA3d 87, 226 CR 199 (covenant restricting residents to persons age 45 and older held invalid under CC §53). As long as one "senior citizen" resides in a dwelling unit, persons who are deemed "qualified permanent residents" may also reside there. CC §51.3(c). Under CC §51.3(b)(3), these include:

- A person age 45 or older, or a spouse, cohabitant, or person providing primary physical or economic support to the senior citizen and residing with the senior citizen before death, hospitalization, or other prolonged absence of, or dissolution of marriage with, the senior citizen; or
- A child or grandchild of the resident (senior citizen or qualified permanent resident) who needs to live with that resident as a result of a physical or mental disability as defined in CC §54(b) or who has a condition that results in such a disability.

For further discussion of senior citizen housing, see Forming California Common Interest Developments §§7.107-7.115 (Cal CEB 2004).

© The Regents of the University of California

D. Other State Antidiscrimination Laws

§6.104 1. Residential Facilities and Family Day Care Homes

By statute, a residential facility for the elderly serving six or fewer persons is deemed to be a residential use of property by a single family. Health & S C §1569.87. Therefore, recorded covenants that permit only residential use of property cannot be applied to preclude use as a residential facility for the elderly. *Broadmoor San Clemente Homeowners Ass'n v Nelson* (1994) 25 CA4th 1, 8, 30 CR2d 316. See Health & S C §1569.2(k) (defining "residential care facility for the elderly").

Similarly, Health & S C §1597.40 provides that restrictions on the acquisition, use, and occupancy of real property as a family day care home for children are void. See *Barrett v Dawson* (1998) 61 CA4th 1048, 71 CR2d 899 (statute may be applied retroactively). See also Health & S C §1596.78 (definition of "family day care home").

© The Regents of the University of California

§6.105 2. Disabled Access to Condominiums

The Davis-Stirling Common Interest Development Act (CC §§1350-1378), which regulates common interest developments in California, permits a unit owner in a condominium (but not in any other form of common interest development) to modify the unit, at the owner's expense, to facilitate access for persons who are blind, visually handicapped, deaf, or physically disabled. CC §1360(a)(2).

© The Regents of the University of California

§6.106 E. Local Ordinances

Neither the federal nor the state fair-housing scheme is exclusive. Local jurisdictions may prohibit discrimination against classes of persons that are not covered by such laws. See, *e.g., Rolon v Kulwitzky* (1984) 153 CA3d 289, 291, 200 CR 217 (upholding local ordinance prohibiting discrimination based on sexual orientation before that class was added to the Unruh Act (CC §51)).

© The Regents of the University of California

§6.106A VIII. SALE OF DISTRESSED PROPERTY

The recent economic downturn has resulted in an unparalleled number of distressed sales of residential real property. The combination of reckless lending practices, overinflated property values, and widespread refinancing to "cash out" accrued equity left an unprecedented number of homeowners with little, if any, economic stake in their property. When property values then plummeted, their homes or investment properties became worth less than the outstanding amount of their loan(s) or they could not afford their mortgage payments either after their loan rate(s) adjusted up or because of a job loss. In lieu of foreclosure, which has an adverse credit impact on the defaulted borrower and is costly to the secured lender, several transaction structures designed to facilitate the transfer and sale of distressed property have again become prominent, as has concern about unscrupulous practices designed to take advantage of elderly and financially unsophisticated property owners who face foreclosure.

The following sections briefly look at transaction structures designed to transfer or sell property in lieu of foreclosure: the "deed in lieu of foreclosure" (§6.106B), the "short sale" (§6.106C), and the home equity sales contracts (§6.107). In addition, §6.110 discusses unique issues that arise in the post-foreclosure sale of bank-owned ("REO") property. For a more in-depth treatment of foreclosure, including debtor's strategies in dealing with foreclosure and bankruptcy issues, see California Mortgages, Deeds of Trust, and Foreclosure Litigation, chaps 7, 10, 12 (4th ed Cal CEB 2009).

© The Regents of the University of California

§6.106B A. Deeds in Lieu of Foreclosure

One strategy for avoiding foreclosure is for the borrower to deed the property back to the lender by delivering a "deed in lieu of foreclosure" or "deed in lieu." For delivery of the deed to be effective, the lender must accept the deed. *Perry v Wallner* (1962) 206 CA2d 218, 222, 23 CR 352. Acceptance may be evidenced by the lender's retention or recordation of the deed. A lender that rejects the conveyance may effectively do so by recording a notice of nonacceptance of the deed. CC §1058.5.

Delivery of a deed in lieu does not extinguish the note or deed of trust and, unlike foreclosure, does not extinguish junior liens. Because junior liens survive, a lender is most likely to be amenable to accepting a deed in lieu when there are no junior liens or the junior liens are held by the same lender. A deed in lieu transaction benefits the lender by avoiding the cost, delay, and uncertainty of foreclosure proceedings. On the other hand, the lender who accepts a deed in lieu becomes subject to the rights of any junior lienholders and risks being subject to subsequent actions by the borrower or its creditors to set aside the conveyance. *Streiff v Darlington* (1937) 9 C2d 42, 68 P2d 728.

From the borrower's perspective, a deed-in-lieu transaction is beneficial to the extent it stops foreclosure proceedings, may be less injurious to the borrower's credit rating than foreclosure, and eliminates the borrower's exposure to a possible deficiency judgment (when applicable). On the other hand, the transaction may expose the borrower to income tax liability to the extent of the forgiveness of the underlying debt (except when the debt is non-recourse under CCP §580b) as well as capital gains tax liability. Therefore, it is essential that the tax consequences of a particular transfer by deed in lieu be evaluated by a qualified tax professional. Moreover, it is generally advisable that the transaction be documented, including an agreement by the lender to accept the deed in lieu, cancel the underlying note, and reconvey the deed of trust.

For a detailed discussion of deeds in lieu (including a form), see California Mortgages, Deeds of Trust, and Foreclosure Litigation §§7.2-7.21, §§10.28-10.32 (4th ed Cal CEB 2009).

© The Regents of the University of California

§6.106C B. Short Sales

"Short sale" refers to a transaction in which a secured lender agrees to accept less than the outstanding loan balance as full satisfaction of the loan obligation. The lender has no obligation under the note, deed of trust, or otherwise to entertain a proposed short sale. As with a deed in lieu (§6.106B), the lender's primary incentive for doing so is to avoid the cost, delay, and uncertainty of foreclosure proceedings and the subsequent ownership, marketing, and sale of the property. A deed-in-lieu transaction is beneficial to the borrower to the extent it stops foreclosure proceedings, may be less injurious to the borrower's credit rating, and eliminates the borrower's exposure to a possible deficiency judgment.

PRACTICE TIP: Typically, a lender will report a short sale to credit agencies as settlement of a financial obligation for less than the full balance. In addition, a lender may have reported one or more late payments made by the borrower before the short sale. Therefore, a borrower's credit will generally be adversely affected by a short sale. A borrower may request that the lender not report the short sale to credit agencies, but the lender has no obligation to agree not to do so.

© The Regents of the University of California

§6.106D 1. Standard Forms Used; Disclosure Requirements Apply

A short-sale transaction is like any other residential transaction between a buyer and seller. The parties may use a standard form purchase contract (*e.g.,* CAR Form RPA-CA). See §6.24. CAR has drafted a "Short Sale Addendum" to Form RPA-CA (CAR Form SSA), which should also be used. See §6.28A. The lender is not a party to the purchase contract. Rather, as set forth on the Addendum, the purchase contract is made contingent on receiving written consent from all existing lienholders to the terms of the proposed short sale by a date certain. This consent includes an agreement by all lienholders to accept, as satisfaction of the outstanding loans, the net proceeds from the parties' agreed purchase price less all seller monetary obligations agreed to in the purchase contract, including payment of attendant costs, such as brokerage commissions, real property taxes, and closing costs. The Addendum also advises the seller that the short-sale transaction may have adverse credit and legal consequences and may result in taxable income to the seller.

NOTE: A short sale is not exempt from any of the seller disclosure obligations imposed by common law or statute. Moreover, the buyer has the same duty to inspect the property, even though, practically speaking, the seller is unlikely to agree to correct deficiencies in the property.

© The Regents of the University of California

§6.106E 2. Lender's Evaluation and Requirements

A lender's agreement to a short sale is strictly a business decision; the lender is under no legal obligation to accept less than full repayment of the outstanding debt. In evaluating a short sale proposal, lenders typically consider the current market value of the property as compared with the amount of the proposed short-sale payoff, market conditions in the area where the property is located, the borrower's financial situation, and evidence that the buyer is capable of performing quickly (such as a cash buyer or loan-preapproved buyer who is offering a short escrow period with few, if any, contractual contingencies).

Lenders typically will require the seller to submit substantial documentation to establish his or her financial distress, including a written statement of hardship, tax returns, paycheck stubs, bank statements, and other financial information. In addition, lenders will require information about the transaction, including the purchase contract, title report, escrow instructions, and estimated settlement statement.

NOTE: Until January 1, 2014, beneficiaries of deeds of trust must prepare and deliver a short-pay demand statement within 21 days of receiving a short-pay request from an entitled person. The short pay statement must set forth an amount less than the outstanding debt, together with any terms and conditions, under which the beneficiary will execute and deliver a reconveyance of the deed of trust. A beneficiary who elects not to proceed with the proposed transaction may refuse to provide a short-pay demand statement but must provide a written statement within 21 days indicating that it has elected not to proceed with the transaction. CC §2943.

© The Regents of the University of California

§6.106F 3. Tax Considerations

The tax implications of a short sale, like a deed-in-lieu transaction, are complicated and will vary depending on the unique facts and circumstances of each case. Therefore, a seller's decision to propose a short sale should follow a qualified tax professional's careful evaluation of the tax implications to the seller. Among other things, a short sale may result in ordinary income or capital gain to the seller. For example, the difference between the outstanding loan balance and the lesser net amount the lender agrees to accept as payment in full is treated as "cancellation of debt," which is generally taxable as ordinary income. This could make a short sale undesirable, particularly when a substantial amount of the loan balance is forgiven.

There are certain important exceptions to this general rule, including the exception set forth in IRC §108(a)(1)(E), added as part of the Mortgage Forgiveness Debt Relief Act of 2007 (Pub L 110-142). Under the Act, discharge of indebtedness income will not be taxed if:

- The property sold is the taxpayer's principal residence (IRC §121);
- The debt is "qualified principal residence indebtedness" (IRC §108(h)(2) (a loan used to acquire, construct or substantially improve a residence); and
- The debt discharge (up to certain maximum amounts) occurred between January 1, 2007 and January 1, 2013. IRC §108(a)(1)(E).

Because this exemption only applies to "purchase money" loans, however, a short sale involving a refinanced loan would not qualify for the exception.

In addition, the short-sale seller may be exposed to capital gains tax in connection with the transaction. In that regard, the amount that is exempt from taxation as ordinary income under IRC §108(a)(1)(E) is applied to reduce the taxpayer's basis of the subject property. IRC §108(h). Therefore, a short-sale seller may face a substantial capital gains tax liability, subject to the exclusion of up to $250,000 (if single) or $500,000 (if married) that applies to the sale of a principal residence.

NOTE: SB 1055, enacted in 2008, conforms Revenue and Taxation Code §17144.5 to the Mortgage Forgiveness Debt Relief Act of 2007 except that the California statute applies only to property sold on or after January 1, 2007, and before January 1, 2009, and specifies lower limits on the maximum amount of debt forgiveness.

© The Regents of the University of California

§6.107 C. Home Equity Sales Contracts

The Home Equity Sales Contracts Act (CC §§1695-1695.17) governs certain residential sale transactions entered into between the commencement of foreclosure proceedings and the date of a foreclosure sale. The Act is supported by legislative findings that homeowners whose residences are in foreclosure, especially the poor, elderly, and financially unsophisticated, are often vulnerable to people who seek to purchase the homeowner's equity between the commencement of foreclosure proceedings and the date of the foreclosure sale ("equity purchasers"). Typically, these equity purchasers will, through schemes involving oral and written misrepresentation, deceit, and intimidation, induce homeowners to sell their homes at prices far below the fair market value. See CC §1695 (legislative findings and declaration). By definition, "equity purchasers" do not include persons who purchase the property for use as a personal residence, or who acquire title by deed in lieu, trustee's sale, or other statutory sale, by order or judgment of a court, or from a spouse, blood relative, or blood relative's spouse. CC §1695.1(a). See *Spencer v Marshall* (2008) 168 CA4th 783, 85 CR3d 752. An "equity seller" is the seller of a "residence in foreclosure" (a residential one to four unit dwelling, of which the equity seller occupies one unit as his or her principal residence and against which an outstanding notice of default is recorded). CC §1695.1(b), (c). See *In re Phelps* (2001) 93 CA4th 451, 113 CR2d 217 (legislature intended regulation of home equity sales contracts to apply only to owner-occupied property). Contracts, agreements, offers, and other arrangements between equity purchasers and equity sellers are home equity sales contracts subject to the Act. CC §1695.1(e).

For further discussion regarding the Home Equity Sales Contract Act, see California Real Property Remedies and Damages §4.63 (2d ed Cal CEB 2002).

© The Regents of the University of California

§6.108 1. Requisites for Enforceability

A home equity sales contract must meet certain formal requirements to be enforceable. It must be written in at least 10-point bold type in the language principally used by the home equity seller and must be fully executed and dated before execution of any instrument conveying the property. CC §1695.2. The contract must contain certain specified provisions (CC §1695.3), including two statutory notices regarding the equity seller's 5-day cancellation right, which must meet specified font size and type requirements and be placed in immediate proximity to the space reserved for the equity seller's signature. CC §§1695.3(g)-(h), 1695.5(a). The contract must also attach a form of notice of cancellation, although the equity seller need not use this form for a cancellation to be effective. CC §§1695.4(c), 1695.5(b).

The equity purchaser must provide the equity seller with a copy of the contract, attaching the notice of cancellation. CC §1695.5(c). Until the equity purchaser provides the copy of the contract and notice, the equity seller may cancel the contract. CC §1695.5(d).

© The Regents of the University of California

§6.109 2. Prohibited Conduct and Remedies

During the equity seller's 5-day cancellation period, the equity purchaser may not take any deed from the equity seller, record any document, transfer or encumber the property, or pay the equity seller any consideration. CC §1695.6(b). If the equity seller delivers notice of cancellation of contract, the equity purchaser must, within 10 days of receipt, return without condition the contract and any other documents signed by the equity seller. CC §1695.6(c). The equity purchaser cannot make untrue or misleading statements about the value of the property, the foreclosure proceeds the equity seller will receive, the equity seller's rights related to the transaction, or the transaction documents or terms. CC §1695.6(d). If the equity purchaser takes title to the property while purporting to give the equity seller an option to repurchase the property, the equity purchaser is prohibited from encumbering or transferring the property or any interest in it without the equity seller's written consent. CC §1695.6(e). Moreover, such a purported absolute conveyance will be presumed to be a mortgage and the transaction a loan; however, the presumption will not apply to a bona fide purchaser or encumbrancer for value who does not have notice of a violation of the home equity sales contract law, even if he or she knows the property was an owner-occupied residential foreclosure. CC §1695.12.

An equity purchaser who commits any of the prohibited acts set forth in CC §1695.6, or who otherwise engages in fraudulent or deceitful conduct, is liable on conviction for a fine of not more than $25,000 or imprisonment for not more than 1 year, or both, for each violation. CC §1695.8. An equity seller may recover damages and other equitable relief against the equity purchaser, plus attorney fees and costs. In addition, an equity seller may be awarded exemplary damages for certain violations, or a civil penalty of up to $2500, but not both. CC §1695.7; see *Boquilon v Beckwith* (1996) 49 CA4th 1697, 57 CR2d 503 (attorney fees not available for time not reasonably spent).

In addition, it is unlawful for any person to negotiate, enter into, or consummate a transaction with an equity seller involving property in foreclosure on terms that take unconscionable advantage of the equity seller. CC §1695.13. Such a transaction is voidable and may be rescinded by the property owner, within 2 years of recordation of the conveyance, by delivering a notice of rescission to the equity purchaser and recording such notice; however, the property owner cannot rescind a transaction with a bona fide purchaser or encumbrancer for value if the purchase or encumbrance occurred before recordation of the notice of rescission. CC §1695.14.

© The Regents of the University of California

§6.110 D. Bank-Owned (REO) Sales

An "REO" (real estate owned) sale refers to the sale of real property owned by a bank. Typically, the bank acquires the property by foreclosure or deed in lieu. An REO sale is like any other residential real estate transaction except that the seller is a financial institution rather than an individual owner-occupant or investor. Although the bank is not distressed in the same sense as a borrower in default, the bank generally is similarly motivated to close a transaction quickly, perhaps at a discounted purchase price.

The process of contracting in an REO sale can be complicated. Most lenders insist on using their own custom purchase contracts, which often are drafted for national use. These lender contracts often are not customized to California requirements and/or may otherwise contain seller-oriented provisions that are undesirable. Local real estate agents who are familiar with the CAR forms or other locally used standard contract forms are not qualified, or legally permitted, to advise buyers on these custom contract forms. Therefore, an attorney's involvement is essential. Further complicating matters, the bank's listing agent often requests that purchase offers be submitted on the CAR or local customary contract form along with an executed addendum prepared by the lender. The addendum typically provides that its terms govern any conflict with the CAR form (and there often are many). Nevertheless, lenders are typically reluctant or unwilling to negotiate any of the terms of their form contracts.

PRACTICE TIP: Depending on market conditions and the particular lender involved, it may be possible to negotiate certain terms of the lender's REO purchase contract or at least prepare an addendum that resolves inconsistencies between provisions in the standard form contract and the lender's custom addendum. As in any negotiation in which the other side has the stronger bargaining position, newly proposed or revised terms are more likely to be considered if they are limited in number and clearly and succinctly drafted.

REO sales are generally exempt from the transfer disclosure requirements if the property was acquired by the bank by foreclosure, deed in lieu, or at a trustee's sale. See §6.35. As such, the bank need not provide a Real Estate Transfer Disclosure Statement (TDS) (see §§6.36-6.37), a Natural Hazard Disclosure Statement (NHDS) (see §§6.49-6.50), or any other disclosure that is required when a TDS is required. The bank is not exempt, however, from certain statutorily mandated disclosures, including the smoke detector and water heater compliance disclosures (see §§6.57-6.58), Megan's Law database disclosure (see §6.56), federal lead-based paint disclosure (see §6.51), and certain natural hazard zone disclosures (although use of the statutory NHDS is not required). Moreover, as the property owner, the bank is subject to the common law duty to disclose known material facts affecting the value or desirability of the property (see §§6.30-6.33). This includes facts about the property contained in the bank's records or known to its employees and agents. See §6.30. CAR has published an REO Advisory, which informs buyers about the unique contractual and disclosure issues in REO sales. See form in §6.111.

Agents of a lender often discover material information about an REO property during the course of managing and marketing it for sale. In addition, the defaulted borrower or tenants at the property often inform one of the lender's agents of defects and other property conditions that should be disclosed. Lenders often disclaim any knowledge about the property condition. But that is irrelevant to the question whether the lender, through its agents, has discovered material information that gives rise to a duty of disclosure. Like any seller, an REO lender-seller is subject to liability for fraud for failure to disclose, or concealment of, known material facts.

PRACTICE TIP: Some lenders, in an effort to minimize exposure to fraud claims, have included onerous provisions in their required transaction documents, including broad "as is" clauses and liability releases, which are likely unenforceable in California or at the very least ineffective to waive or limit common law disclosure duties. It is therefore advisable for buyers of REO property to consult with an attorney regarding the terms of lender-drafted purchase agreements. Ultimately, it is advisable for buyers of REO properties to conduct a high level of due diligence, including thorough pest and home inspections, careful review of title information and public records, interviews of representatives of any homeowners' association and review of HOA records, as well as interviews of any current or former occupants of the property and neighbors.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/6 Residential Purchase and Sale Transactions/ §6.111 E. Form: REO Advisory (CAR Form REO)

§6.111 E. Form: REO Advisory (CAR Form REO)

Print

CALIFORNIA ASSOCIATION OF REALTORS ®

REO ADVISORY
For Properties Being Sold by a Lender After Foreclosure
(C.A.R. Form REO, 4/08)

Property Address: _____ ("Property").
The Seller of the Property is a lender who has acquired title to the Property either by foreclosure or through a deed given in lieu of foreclosure. Many obligations imposed upon sellers, particularly sellers of real property containing one-to-four dwelling units, may not be applicable to the sale of the Property. However, even though Seller is exempt from many obligations, Seller must still comply with many others. Further, even though a Seller may be exempt from certain obligations, a real estate broker's obligations may still apply. This Advisory is intended to inform Buyer and Seller of their rights and obligations independent of those established by the contract between them.

EXEMPTIONS:

1. **TDS, NHD, Mello-Roos, Improvement Bond Act, Supplemental Property Taxes, Private Transfer Fee:** Seller is exempt from providing Buyer with the Real Estate Transfer Disclosure Statement (TDS), Natural Hazard Disclosure Statement (NHD), a Mello-Roos district lien disclosure, an Improvement Bond Act of 1915 notice, a Supplemental Property Tax notice, and a Notice of Private Transfer Fee pursuant to California Civil Code §§ 1102 et seq.

2. **Earthquake Guides:** Seller is exempt from providing either a Homeowner's or Commercial Property Owner's Guide to Earthquake Safety.

REQUIREMENTS:

1. **Disclosures:** Seller is not exempt from common law and statutory duties concerning fraud and deceit, even though the specific TDS Form is not required to be completed. Seller remains obligated to disclose known material facts affecting the value and desirability of the Property.

2. **Hazard Zones:** Seller is not exempt from applicable statutory obligations to disclose earthquake fault zones, seismic hazard zones, state fire responsibility areas, very high fire hazard severity zones, special flood hazard areas and flood hazard zones pursuant to the Public Resources Code, Government Code and United States Code, even though, pursuant to the Civil Code, the specific NHD Form is not required to be completed.

3. **Smoke Detectors:** The sale is not exempt from the State requirements that, for single family residences, operable smoke detectors be in place and that a written statement of compliance be provided to Buyer. It is negotiable between Buyer and Seller who is to pay for the cost of compliance.

4. **Water Heaters:** The sale is not exempt from the State requirement that water heaters be properly anchored, braced or strapped and that Seller provide a written statement of compliance to Buyer. It is negotiable between Buyer and Seller who is to pay for the cost of compliance.

5. **Lead-based Paint:** The Seller is not exempt from the federal obligation to: **(i)** disclose known lead-based paint and lead-based paint hazards; **(ii)** provide Buyer copies of reports or studies covering lead-based paint and hazards on the Property; **(iii)** provide Buyer with the pamphlet "Protect Your Family From Lead In Your Home;" and **(iv)** give Buyer a 10-day opportunity to inspect for lead-based paint and hazards, if the Property contains residential dwelling units and was constructed prior to 1978.

The copyright laws of the United States (Title 17 U.S. Code) forbid the unauthorized reproduction of this form, or any portion thereof, by photocopy machine or any other means, including facsimile or computerized formats. Copyright © 2008, CALIFORNIA ASSOCIATION OF REALTORS®, INC. ALL RIGHTS RESERVED.

Buyer's Initials (_____)(_____)
Seller's Initials (_____)(_____)
Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

SAMPLE

Print

Property Address: _____ Date: _____

6. **Megan's Law Database Disclosure:** The sale is not exempt from the requirement that residential sales contracts contain the following notice regarding the availability of information about registered sex offenders. "Notice: Pursuant to Section 290.46 of the Penal Code, information about specified registered sex offenders is made available to the public via an Internet Web site maintained by the Department of Justice at www.meganslaw.ca.gov. Depending on an offender's criminal history, this information will include either the address at which the offender resides or the community of residence and ZIP Code in which he or she resides." (Neither Seller nor Brokers are required to check this website. If Buyer wants further information, Broker recommends that Buyer obtain information from this website during Buyer's inspection contingency period. Brokers do not have expertise in this area.)

7. **Tax Withholding:** The sale is not exempt from providing information pertaining to the withholding obligation under either the federal "FIRPTA" or the California withholding requirements upon the sale of real property. However, an REO Seller which is a corporation or limited liability company, formed within the United States, and either qualified with the Secretary of State to do business in California or with a permanent place of business in California, will be exempt from withholding under both Federal and California law.

8. **Brokers:**
   A. Inspection: The sale is not exempt from the Broker's obligation to conduct a reasonably competent and diligent visual inspection of the accessible areas of the Property and disclose to Buyer material facts revealed by such an inspection in the sale of residential property containing one-to-four dwelling units. Brokers may do so on C.A.R. Form AVID.

   B. Agency: The sale is not exempt from the obligation to provide agency relationship disclosure and confirmation forms in the sale of residential property containing one-to-four dwelling units.

OTHER CONSIDERATIONS:

1. **Local Law:** Local law may impose obligations on the transfer of real property (such as the installation of low flow toilets or shower heads, emergency gas shut-off valves or installation of smoke detectors). Local law should be consulted to determine if sales of Lender-owned property are exempt from such requirements.

2. **Amendments to Contract:** Lender-prepared addenda, amendments, or counter-offers to a Buyer and Seller Agreement, or a Lender-Prepared contract may conflict with, contradict or be inconsistent with terms in Buyer's offer. Brokers cannot advise Buyer or Seller: **(i)** which specific terms in any offer may be affected; **(ii)** whether the terms in any such lender-prepared documents are permissible under California Law; or, **(iii)** in the event of a discrepancy between the Lender-prepared documents and the Buyer-Seller Agreement, which document or which terms may supercede the other. Buyer is advised to seek legal counsel to discuss the applicability and interpretation of any lender-prepared documents prior to signing any such documents.

By signing below, the undersigned acknowledge that each has read, understands and has received a copy of this REO Advisory.

Buyer _____ Date _____

Buyer _____ Date _____

Seller _____ Date _____

Seller _____ Date _____

SAMPLE

THIS FORM HAS BEEN APPROVED BY THE CALIFORNIA ASSOCIATION OF REALTORS® (C.A.R.). NO REPRESENTATION IS MADE AS TO THE LEGAL VALIDITY OR ADEQUACY OF ANY PROVISION IN ANY SPECIFIC TRANSACTION. A REAL ESTATE BROKER IS THE PERSON QUALIFIED TO ADVISE ON REAL ESTATE TRANSACTIONS. IF YOU DESIRE LEGAL OR TAX ADVICE, CONSULT AN APPROPRIATE PROFESSIONAL.

This form is available for use by the entire real estate industry. It is not intended to identify the user as a REALTOR®. REALTOR® is a registered collective membership mark which may be used only by members of the NATIONAL ASSOCIATION OF REALTORS® who subscribe to its Code of Ethics.

Published and Distributed by:
REAL ESTATE BUSINESS SERVICES, INC.
a subsidiary of the California Association of REALTORS®
525 South Virgil Avenue, Los Angeles, California 90020

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

© The Regents of the University of California

7

Hazardous Waste Considerations

Kenneth S. Kramer
William D. Wick

I. TOXIC CONTAMINATION
A. Introduction §7.1
B. What Is Toxic Contamination?
1. Frequently Encountered Toxics §7.2
a. Soil Contamination §7.3
b. Groundwater Contamination §7.4
c. Building Contamination §7.5
d. Storage Tanks §7.6
e. Air Quality §7.7
2. Legal Definitions of Toxics
a. Federal Statutes §7.8
b. California Statutes §7.9
C. Remediation Obligations and Defenses §7.10
1. Potentially Responsible Parties §7.11
a. Owners §7.12
b. Lessees as "Owners" §7.13
c. Operators, Arrangers, Transporters §7.14
2. Remediation Orders §7.15
3. Cost Recovery and Contribution §7.16
a. Parties Eligible for Cost Recovery Actions §7.17
b. Liability and Damages Issues §7.18
c. Attorney Fees §7.19
d. Common Law Actions §7.20
4. Private Agreement Limitations §7.21
5. CERCLA Defenses §7.22
a. The Third Party Defense §7.23
b. The Innocent Landowner Defense §7.24
(1) Requirements to Qualify for Innocent Landowner Status §7.25
(2) Application to Property Purchased Before May 31, 1997 §7.26
(3) Application to Property Purchased Between May 31, 1997, and November 1, 2006 §7.27
(4) Application to Property Purchased On or After November 1, 2006 §7.28
(5) Comparison of "All Appropriate Inquiries" Standards §7.29
c. The Contiguous Property Owner Defense §7.30
d. The Bona Fide Prospective Purchaser Defense §7.31
6. California Land Reuse and Revitalization Act of 2004 §7.32
a. Eligible Property §7.33
b. Bona Fide Purchaser §7.34
c. Immunity From Cleanup Costs §7.35
D. Investigation and Review of Environmental Conditions
1. California Toxic Disclosure Statutes §7.36
2. Environmental Assessments
a. Phase I Reports §7.37
b. Phase II Reports §7.38
c. Remedial Investigation/Feasibility Study/Remedial Action Plan §7.39
3. Seller's Review of Property §7.40
4. Buyer's Review of Property §7.41
5. Use of Environmental Consultants
a. Scope of Work §7.42
b. Confidentiality §7.43
c. Principal-Agent Considerations §7.44

II. CONTRACTUAL PROVISIONS ON TOXIC CONTAMINATION §7.45

A. Seller's Documentation of Knowledge
1. Disclosure of Knowledge §7.46
2. Representations and Warranties §7.47
a. Form: Definition of "Hazardous Materials" §7.48
b. Form: Absolute Representation §7.49
c. Form: Best of Knowledge §7.50
d. Form: Best of Knowledge (Specific Individuals) §7.51
e. Form: Best of Knowledge With Exception for Phase I Report §7.52
B. Buyer's Rights Regarding Unknown Contamination §7.53
1. Conditions Precedent for Due Diligence §7.54
2. Lessee's Estoppel Provision §7.55
3. Seller's De Minimis Obligation to Remediate §7.56
4. Form: Seller to Remediate De Minimis Contamination §7.57
5. Rights to Terminate §7.58
6. Loan Contingency Relationship §7.59
C. Renegotiation of Price or Other Terms When Undisclosed Toxics Are Found §7.60
D. Release Clauses §7.61
1. Form: Broad Clause Releasing Seller §7.62
2. Form: Limited Clause Releasing Seller; Seller Retains Some Responsibilities §7.63
3. "As Is" Clauses as Release Clauses §7.64
4. Form: Expanded "As Is" Clause §7.65
E. Indemnification §7.66
1. Seller's Indemnification of Buyer
a. Factors to Consider §7.67
b. Form: Seller's Limited Indemnification of Buyer §7.68
2. Buyer's Indemnification of Seller
a. Assumed Toxic Condition §7.69
b. Form: Buyer's Broad Form Indemnification of Seller §7.70
c. Postclosing Discoveries
(1) Preexisting Conditions §7.71
(2) Conditions Caused by Buyer After Closing §7.72
F. Remediation §7.73
1. Responsibility for Costs §7.74
2. Control of Process §7.75
3. Disposal §7.76
4. Agency Assurances—Comfort Letter and Prospective Purchaser Agreement §7.77
G. Securing Remediation Costs
1. Remediation Cost Estimate §7.78
2. Escrow of Funds §7.79
3. Form: Remediation Escrow Agreement §7.80
4. Letters of Credit §7.81
5. Guaranty §7.82
6. Offset Against Buyer's Note §7.83
H. Miscellaneous Provisions
1. Arbitration Clause §7.84
2. Access to Property §7.85

III. INSURANCE MATTERS
A. Title Insurance Products §7.86
B. Environmental Liability Insurance §7.87

IV. LENDER CONCERNS
A. Nature of Lender's Liability and Underwriting §7.88
B. Loan Application Provisions §7.89
C. Loan Document Provisions §7.90
1. Representations §7.91
2. Assurances on Remediation §7.92
3. Right to Waive Security §7.93
4. Access, Right to Remediate, and Receivership §7.94
5. Survival of Indemnities and Other Agreements After Foreclosure §7.95

© The Regents of the University of California

I. TOXIC CONTAMINATION

§7.1 A. Introduction

Concern about toxic contamination has become a primary issue in acquiring, selling, and leasing real property. In representing a client in a purchase and sale or lease transaction, the attorney must be able to guide the client through the toxic investigation and evaluation process and negotiate a buyer's or seller's (or lessor's or lessee's) rights and obligations regarding toxic contamination that may exist on or under a parcel of land or in a building.

This chapter is not intended to be a thorough review of the statutes and cases related to toxic contamination. Rather, it is an overview of the issues that most real property attorneys are likely to encounter (1) in dealing with toxic contamination as part of a real property purchase and sale or lease transaction and (2) in seeking to protect a client from unexpectedly finding that it owns a contaminated parcel of property or building. This chapter is also not intended to address the California Environmental Quality Act (CEQA) (Pub Res C §§21000-21177) or the federal or California Endangered Species Acts (16 USC §§1531-1544; Fish & G C §§2050-2116) and their effect on a purchase of property. These Acts may, however, be of concern in particular transactions. For a complete discussion of CEQA, see Practice Under the California Environmental Quality Act (2d ed Cal CEB 2008).

A typical real property purchase and sale transaction, and many lease transactions, involve three phases related to toxics:

- Investigation of the property for toxic contamination;
- Evaluation of the extent and nature of the contamination; and
- Negotiation and documentation of each party's rights and responsibilities regarding toxic contamination and its remediation or removal.

The investigation and evaluation (or due diligence) process, including the use of consultants, documenting the seller's disclosures, and addressing due diligence issues, is discussed in §§7.36-7.59. Allocation of the parties' respective rights and responsibilities regarding toxic contamination and documentation of the negotiated allocation are discussed in §§7.60-7.85.

Although for simplicity this chapter uses the terms "toxic contamination" or merely "contamination," these are inexact terms that generally refer to any number of chemicals, substances, or by-products defined variously as hazardous wastes, hazardous substances, and petroleum fractions. The latter terms are defined in the statutes referred to in §§7.8-7.9. Other terms used in this chapter may also be defined in the statutes discussed in this chapter:

- "Release" (defined in 42 USC §9601(22));
- "Response" (defined in 42 USC §9601(25)); and
- "Removal," "remedy," and "remedial action" (defined in 42 USC §9601(23)-(24)).

Most practitioners use the term "remediation" instead of the statutory terms "remedy" or "remedial action," and in practice "remediation" is often used to include both "remedial actions" and "removal," even though their statutory definitions are mutually exclusive.

For additional discussions of toxic issues in buying or leasing real property, see Finkelstein, Hansen & Steel, *Buying Contaminated Property: How to Avoid a Toxic Surprise*, 6 Cal Real Prop J 1 (Spring 1988); Finkelstein, *An Overview of Environmental Considerations Before You Buy or Lease Commercial Real Property*, 7 Cal Real Prop J 1 (Spring 1989); and Environmental Aspects of Real Estate Transactions, Section of Natural Resources, Energy, and Environmental Law and Section of Real Property, Probate, and Trust Law, American Bar Association (1995); Gerrard, Brownfields Law and Practice: The Cleanup and Redevelopment of Contaminated Land (1998); Moskowitz, Environmental Liability and Real Property Transactions: Law & Practice (2d ed 1995); Geltman, Prospective Purchaser Agreements: Reducing the Liability Risks of Contaminated Property (1997).

© The Regents of the University of California

B. What Is Toxic Contamination?

§7.2 1. Frequently Encountered Toxics

The common types of toxic contamination are best categorized in terms of the portion of the property that is affected, *e.g.,* soil (see §7.3), groundwater (see §7.4), or buildings (see §7.5). A contamination problem may affect any or all categories. In addition, underground storage tanks and air quality issues may require special attention (see §§7.6-7.7).

© The Regents of the University of California

§7.3 a. Soil Contamination

Soil can become contaminated from any number of sources, including leakage from underground or aboveground storage tanks, releases of chemicals used in a building on the property, disposal of toxic contaminants on the property, or agricultural pesticide and fertilizer use. Soil contamination can usually be remediated or removed by excavation and disposal, chemical treatment, or bioremediation. A vitrification, or glassification, process that encases contaminated soil in a glasslike substance without removing the soil has also been used in limited circumstances.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/7 Hazardous Waste Considerations/§7.4 b. Groundwater Contamination

§7.4 b. Groundwater Contamination

Releases of toxic contaminants may result in groundwater contamination. Contaminants affecting soil can percolate through the soil to reach groundwater at various depths below the surface, or contaminants leaking from underground tanks or other underground sources can leak directly into the groundwater. The potential for contaminant seepage through the soil to groundwater depends on various factors, including the nature of the contaminant, the porosity of the soil, the depth to groundwater, and the strata in which the release occurred.

When groundwater has been contaminated, the investigation should address whether the contaminated groundwater is limited to an isolated area or whether it is migrating vertically, through the strata above or below the contamination, or horizontally through the groundwater or soil within the contaminated strata. If the contamination is migrating horizontally, treating the problem may require gaining access to adjacent property under which the contaminated groundwater flows in order to install monitoring and remediation facilities. If contamination is migrating vertically, it may affect underground drinking water sources, depending on whether and at what level groundwater is used for drinking water in the area and the strata between the contaminated groundwater and drinking water.

Remediation of groundwater contamination usually requires drilling pumping wells to remove the groundwater and filtering it through systems that remove the contaminants. In limited situations, chemicals can be injected into the groundwater to treat the contamination where it is found. Remediating groundwater contamination usually takes substantially longer than remediating soil contamination.

© The Regents of the University of California

§7.5 c. Building Contamination

Buildings can be contaminated by products used in the construction of the building or by the activities that have occurred in the building. The most common toxic contaminants historically used in the construction of buildings were asbestos-containing materials (ACMs) and polychlorinated biphenyls (PCBs). ACMs were often used as a fire retardant on steel girders and as insulation wrapped around pipes, in ceiling and floor tiles, and in acoustical ceiling spray. Although general use of ACMs as a fire retardant on steel girders continued only until the mid-1970s, other asbestos-containing building materials continued to be used through the 1980s. PCBs are typically found in various electrical equipment, including older fluorescent lamp ballasts.

Inquiries about asbestos should address whether identified ACMs are friable or nonfriable. Friable ACMs, *i.e.*, ACMs that are easily crumbled, are more likely than nonfriable ACMs to result in a release of asbestos fibers into the atmosphere. Nonfriable ACMs can become friable when they deteriorate, and buyers should consider having them removed or encapsulated to avoid asbestos releases. Nonfriable ACMs can often be treated by an in-place maintenance and management program, commonly known as an Operations and Maintenance Program. Although friable ACMs can also be addressed by an Operations and Maintenance Program, almost all buyers require removal. The Environmental Protection Agency (EPA) currently recommends adopting an Operations and Maintenance Program rather than removal for ACMs when such a program is feasible. See Managing Asbestos in Place, A Building Owner's Guide to Operations and Maintenance Programs for Asbestos-Containing Materials, an EPA guidance document issued in 1990.

An owner generally need not remove, or pay a subsequent owner for the cost of removing, ACMs that are part of a building and were installed as building materials in its construction. *3550 Stevens Creek Assocs. v Barclays Bank* (9th Cir 1990) 915 F2d 1355. In *Stevens Creek,* the court found that a buyer of property had no recourse against the seller for the cost of asbestos removal, because the installation of building materials did not require the disposal of a hazardous substance under the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA), as amended (42 USC §§9601-9675). 915 F2d at 1361. For notification requirements regarding released substances and the definitions of "disposal" and "hazardous waste," see 42 USC §§6903, 9601(29). The *Stevens Creek* court further reviewed the legislative history of the Superfund Amendments and Reauthorization Act of 1986 (Pub L 99-499, 100 Stat 1613) and found the following language in the Senate Report to be instructive (915 F2d at 1364):

> Specifically, [the Bill] makes clear the exclusion from remedial or removal action of a release or a threat of a release… from products which are part of the structure of, and result in exposure within a facility….

The analysis in *Stevens Creek* should similarly apply to PCBs.

There are, however, exceptions to this general rule. In *City of Greenville v W.R. Grace & Co.* (D SC 1986) 640 F Supp 559, aff'd (4th Cir 1987) 827 F2d 975, a manufacturer of asbestos-containing Monokote fireproofing materials was found liable to a building owner for the cost of removing the Monokote on theories of negligence and product warranty when the ACMs had fallen off the beams in the building and contaminated it and when the manufacturer was found to have been aware of the risks of asbestos before supplying the Monokote for construction of the building. In *CP Holdings v Goldberg-Zoino & Assocs.* (D NH 1991) 769 F Supp 432, the court held the seller of a hotel liable to the buyer for the cost of asbestos removal when the buyer, with the seller's foreknowledge, demolished the building after the sale. The court held that, because the sellers knew the building would be demolished, the sale of the building constituted "disposal" of asbestos by the sellers. 769 F Supp at 438.

Use of solvents or corrosive chemicals inside a building as part of a manufacturing process, without adequate controls, can result in toxic contamination of parts of the building, such as walls, ceiling tiles, or floors. If the chemicals seep through the floor or are disposed of outside the building, the soil or groundwater below and around the building may also become contaminated. The presence of chemicals is not always apparent. Dust and dirt in a manufacturing facility sometimes contain significant concentrations of contaminants from the manufacturing processes that were housed in the building. Remediation of such contamination typically involves cleaning the surfaces of walls, ceilings, and floors or removing and replacing parts of the building, or both.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/7 Hazardous Waste Considerations/§7.6 d. Storage Tanks

§7.6 d. Storage Tanks

Storage of chemicals and hazardous substances in aboveground or underground tanks is a frequent cause of soil and groundwater contamination. Owing to the frequency of tank leaks and the fact that leakage from underground tanks is often undetected, these tanks are the subject of separate legislation requiring permits for such tanks and periodic testing. 42 USC §§6991-6991m; Health & S C §§25280-25299.206. Buyers who do not intend to use the tanks should consider having them removed before acquiring the property.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/7 Hazardous Waste Considerations/§7.7 e. Air Quality

§7.7 e. Air Quality

Potential buyers may wish to investigate whether the existing or proposed use of a parcel of property could affect air quality, either directly or indirectly. Although residential and office projects are not usually direct sources of air pollution, they may become subject to air quality regulations designed to address indirect sources.

Health and Safety Code §40716 (added in 1988 as part of the California Clean Air Act) authorizes the adoption and implementation of regulations by air quality management or air pollution control districts to reduce or mitigate indirect sources of air pollution. Although §40716 also provides that it is not intended to infringe on the land use authority of cities and counties, many practitioners are concerned that regulation of indirect sources may result in an additional tier of government approvals for California projects. When the regulations cover transportation controls, the districts may delegate that responsibility to city and county governmental agencies that have adopted their own measures. Health & S C §40717(e).

Another portion of the Clean Air Act authorizes the South Coast Air Quality Management District to impose fees on indirect sources of emissions that it regulates. Health & S C §40522.5. Developers and landowners will likely be subject to even further regulation in the effort to control air pollution resulting directly or indirectly from property use, so their counsel should review the rules promulgated by the air quality management district for the area in which the property is located.

© The Regents of the University of California

2. Legal Definitions of Toxics

§7.8 a. Federal Statutes

The primary federal statutes dealing with toxic contamination are the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA) as amended (42 USC §§9601-9675) and the Resource Conservation and Recovery Act of 1976 (RCRA) as amended (42 USC §§6901-6992k). CERCLA generally addresses releases of hazardous substances and the procedures, costs, and responsibilities for remediating or removing such substances, while the RCRA is intended to regulate and ensure appropriate protections on the generation, storage, treatment, transportation, and disposal of hazardous wastes. In most real property purchase and sale transactions, CERCLA is the more important statutory scheme.

CERCLA authorizes the Environmental Protection Agency (EPA) to prepare a list of substances designated as hazardous based on a determination that certain substances, when released into the environment, may present a substantial danger to the public health or welfare or to the environment. 42 USC §9602(a). The substances so designated, as well as other substances designated under or meeting the definitions of other specified federal statutes, are defined as "hazardous substances." 42 USC §9601(14). They include, but are not limited to, hazardous wastes designated under or having the characteristics identified in the RCRA (42 USC §6921) and toxic pollutants listed under the Federal Water Pollution Control Act (33 USC §1317(a)).

Under 42 USC §6921(b), the EPA must identify hazardous wastes that are subject to the RCRA, "taking into account toxicity, persistence, and degradability in nature, potential for accumulation in tissue, and other related factors such as flammability, corrosiveness, and other hazardous characteristics." 42 USC §6921(a). The actual definition of hazardous waste under the RCRA also encompasses the potential for wastes to affect health or the environment. 42 USC §6903(5). Petroleum is expressly excluded from the definition of hazardous substances under CERCLA unless it is otherwise designated as a hazardous substance under one of the other Acts incorporated in the definition by reference. 42 USC §9601(14). The EPA's position, however, is that hazardous substances that are added to petroleum, or that increase in concentration solely because of contamination of petroleum during use, do not come within the petroleum exclusion. See memorandum from EPA General Counsel to EPA Assistant Administrator for Solid Waste and Emergency Response (July 31, 1987). The Ninth Circuit endorsed the EPA's position in *Cose v Getty Oil Co.* (9th Cir 1993) 4 F3d 700, 704. Thus "waste oil" or "used oil" does not fall within the petroleum exclusion.

Despite the general exclusion for petroleum, petroleum leaks are still a concern that must be addressed because of the federal and California underground storage tank statutes, 42 USC §§6991-6991m and Health & S C §§25280-25299.206. For example, 42 USC §6991(2) defines "regulated substance" as all hazardous substances (other than RCRA hazardous wastes) *and petroleum*. Moreover, it was held in *Zands v Nelson* (SD Cal 1991) 779 F Supp 1254 that a civil cause of action exists for leaked petroleum under 42 USC §6972(a)(1)(B), which provides that anyone may commence a civil action on his or her own behalf against anyone "who has contributed or who is contributing to the past or present handling, storage, treatment, transportation, or disposal of any solid or hazardous waste." 779 F Supp at 1262. The court further stated that, although CERCLA "explicitly and specifically excludes petroleum," the RCRA has no petroleum exemption. 779 F Supp at 1263 n6.

NOTE: The terms "hazardous substance" and "hazardous waste" are often used carelessly and may often be intended to refer not only to the CERCLA and RCRA definitions (including other statutes incorporated in those Acts by reference) but to lesser known federal and state statutes and to local ordinances, rules, and regulations on toxic liability and remediation requirements. See definition of hazardous materials in §7.48.

© The Regents of the University of California

§7.9 b. California Statutes

California has adopted two acts that parallel the primary federal statutes: the Carpenter-Presley-Tanner Hazardous Substance Account Act (HSA) (Health & S C §§25300-25395.45), which is often called the California Superfund and, like CERCLA, addresses issues related to releases of toxic contamination, and the Hazardous Waste Control Law (HCL) (Health & S C §§25100-25257.1). The HCL not only parallels the goals and provisions of the Resource Conservation and Recovery Act of 1976 (RCRA), as amended (42 USC §§6901-6992k), but was adopted to be implemented in lieu of the federal program in accordance with the RCRA, which expressly authorized states to adopt in-lieu programs. Health & S C §25101(d); 42 USC §6926.

Not surprisingly, the definitions of "hazardous substance" and "hazardous waste" under the California acts are similar to, and rely in part on, the definitions in the federal acts. Under the HSA, "hazardous substance" is defined to include any hazardous substance designated in accordance with 42 USC §9602, any hazardous waste so defined in 42 USC §6921, certain other substances designated under other federal statutory provisions, and any hazardous waste as defined or designated under the HCL. Health & S C §25316. Petroleum is excluded from the HSA definition of hazardous substance unless it is otherwise specifically designated in one of the code sections incorporated by reference in Health & S C §25316. Health & S C §25317.

The HCL defines hazardous waste in the same terminology as the RCRA definition and expressly incorporates all hazardous wastes so designated under the RCRA. Health & S C §25117. The HCL also requires the State Department of Toxic Substances Control to establish criteria for identifying, and to adopt a list of, hazardous wastes. Health & S C §§25140-25141.

The state underground storage tank statutes have a separate definition of hazardous substance, which differs from the HSA definition in that it includes (in addition to the hazardous substances defined in §25316) regulated substances under 42 USC §6991(2) and materials classified by the National Fire Protection Association as flammable liquids or class II or class III-A combustible liquids. Health & S C §25281(h). These provisions bring petroleum, gasoline, and certain other petroleum fractions that are not normally considered hazardous under the HSA within the California underground storage tank statutes.

© The Regents of the University of California

§7.10 C. Remediation Obligations and Defenses

Toxic contamination is a significant issue in real property transactions because a property owner, operator, or lessee may be required to remediate contamination or may be liable to third parties for their remediation costs, even if the owner or operator did not cause the contamination or no longer owns the property.

The government may seek the imposition of joint and several liability on defendants unable to demonstrate that liability can be apportioned. However, the Supreme Court has held that apportionment among defendants is proper if there is a reasonable basis for determining the contribution of each defendant to a single harm. See *Burlington N. & Santa Fe Ry. Co. v U.S.* (2009) 556 US __, 173 L Ed 2d 812, 129 S Ct 1870. In *Burlington Northern*, the Ninth Circuit had found that the evidence supporting the district court's allocation was insufficient to establish the precise portion of the railroad's liability. In reversing, the Supreme Court held that the evidence need not be precise; there simply must be facts in the record reasonably supporting the apportionment. Here, the district court had used a formula that included the percentage of land leased, the period of ownership, and the types of chemicals spilled.

Defenses to CERCLA liability are limited because CERCLA imposes strict liability. *New York v Shore Realty Corp.* (2d Cir 1985) 759 F2d 1032, 1042; *U.S. v Maryland Bank & Trust Co.* (D Md 1986) 632 F Supp 573, 576. As a result, purchasers and lessees should take reasonable steps to protect themselves from buying or leasing contaminated property, and sellers of potentially contaminated property need to address buyers' concerns.

© The Regents of the University of California

§7.11 1. Potentially Responsible Parties

Among the "potentially responsible parties" (PRPs) who may be responsible for remediation or removal, or for its costs, are owners, operators, owners or operators at the time of disposal, transporters, persons arranging for transportation or disposal, and disposal facility owners and operators. 42 USC §9607(a) (CERCLA); Health & S C §25323.5 (HSA); *U.S. v Maryland Bank & Trust Co.* (D Md 1986) 632 F Supp 573, 577 (current owner may be liable without also being current operator, and vice versa, despite poorly drafted language of 42 USC §9607(a)(1), which refers to "owner and operator").

© The Regents of the University of California

§7.12 a. Owners

Buyers and sellers of real property generally focus on the liability of owners as PRPs. The parties that face liability as owners may include a current owner of the property (whether or not that owner disposed of or contributed to the toxic contamination) or the owner "at the time of disposal." 42 USC §9607(a)(1)-(2). See also *New York v Shore Realty Corp.* (2d Cir 1985) 759 F2d 1032, 1044 ("section 9607(a)(1) unequivocally imposes strict liability on the current owner … without regard to causation"). In *Tanglewood E. Homeowners v Charles-Thomas, Inc.* (5th Cir 1988) 849 F2d 1568, a residential developer was held potentially liable for toxic contamination caused by the prior owner who abandoned the site, and the court denied the developer's motion to dismiss. The developer was found potentially liable both as a current owner, without regard to causation of the problem (849 F2d at 1573), and as a prior owner on the ground that certain of its development activities constituted "disposal."

An owner is liable under CERCLA (42 USC §§9601-9675) unless the owner can demonstrate one of the "innocent landowner" defenses (see §§7.24-7.31). Thus, an owner who did not cause the contamination but who is a potentially liable party is likely to be jointly and severally liable under CERCLA. *U.S. v Burlington N. & Santa Fe Ry. Co.* (9th Cir 2007) 479 F3d 1113, 1136 (case was consolidated and cert granted Oct. 1, 2008) 2008 US Lexis 5437, 171 L Ed 2d 931, 129 S Ct 30 (landowners "typically" cannot prove that costs should be divisible among parties, and are thus jointly and severally liable).

Under CERCLA, prior owners "at the time of disposal of any hazardous substance" are also liable for cleanup costs. 42 USC §9607(a)(2). The Ninth Circuit Court of Appeals has held that, in most situations, the migration of contamination through the soil does not constitute "disposal." *Carson Harbor Village, Ltd. v Unocal Corp.* (9th Cir 2001) 270 F3d 863. Past owners, therefore, who acquired property after an initial deposit of hazardous waste and then sold it are probably not liable parties under CERCLA. The court in *Carson Harbor* held that the passive soil migration was not like a leaking underground storage tank, "or a vessel or some other container that would connote 'leaking.'" 270 F3d at 879. The court concluded, therefore, that there was no disposal, but cautioned that it was "mindful that the statute will be applied in a myriad of circumstances, many of which we cannot predict today.… This approach does not rule out the scenario in which 'spilling,' 'leaking,' or perhaps other terms in some circumstances, encompasses passive migration." 270 F3d at 880.

The practical consequence is that current owners are likely to have fewer past owners to share in any cleanup costs. Thus, environmental due diligence before acquisition is more important than ever.

© The Regents of the University of California

§7.13 b. Lessees as "Owners"

According to most district courts that have considered the question, site control is a sufficient indicator of ownership to impose CERCLA "owner" liability on lessees or sublessors. See, *e.g., Servco Pac., Inc. v Dods* (D Haw 2000) 106 F Supp 2d 1034, 1045 (lessee had sufficient control and possessory interest in property under 50-year lease to be deemed "owner"); *Louisiana v Braselman Corp.* (ED La 1999) 78 F Supp 2d 543, 551 (lessee exercised sufficient control over and responsibility for use of property to be deemed "owner"); *U.S. v A & N Cleaners & Launderers, Inc.* (SD NY 1992) 788 F Supp 1317, 1333 ("The undisputed facts establish that [the sublessor] exercised a degree of site control over the Property, [which] confers ownership status upon it for purposes of CERCLA §107(a)."); *U.S. v South Carolina Recycling & Disposal, Inc.* (D SC 1985) 653 F Supp 984, 1003, aff'd sub nom *U.S. v Monsanto Co.* (4th Cir 1988) 858 F2d 160 ("[The lessee] maintained control over and responsibility for the use of the property and, essentially, stood in the shoes of the property owners.").

The Second Circuit, in holding that a lessee was not an owner in *Commander Oil Corp. v Barlo Equip. Corp.* (2d Cir 2000) 215 F3d 321, 330, set forth five criteria that could render a lessee an "owner" under CERCLA:

- The lease is for an extensive term and the lessor may not determine how the property is used;
- The lessor cannot terminate the lease before it expires by its terms;
- The lessee may sublet all or some of the property without notifying the lessor;
- The lessee is required to pay all taxes, assessments, insurance, and operation and maintenance costs; and
- The lessee is required to make all structural and other repairs.

The Second Circuit noted that this list of factors is "non-exclusive." The guiding principle for the court was whether the lessee is a de facto owner, not whether it exercises control over the premises. 215 F3d at 331.

© The Regents of the University of California

§7.14 c. Operators, Arrangers, Transporters

An owner or lessee may also be liable as an "operator," "arranger," or "transporter" of hazardous substances. 42 USC §9607. *Tanglewood E. Homeowners v Charles-Thomas, Inc.* (5th Cir 1988) 849 F2d 1568, 1573. Moreover, officers or directors may be personally liable under CERCLA and California law if the person had control over the day-to-day management and operation of the facility that released the hazardous substances. *California Dep't of Toxic Substances Control v Celtor Chem. Corp.* (ND Cal 1995) 901 F Supp 1481.

© The Regents of the University of California

§7.15 2. Remediation Orders

If there "may be an imminent and substantial endangerment to public health or welfare or the environment," the President may order a party to take remedial action to abate or remediate a release or to cause the Attorney General to seek an injunction requiring remediation. 42 USC §9606(a); *U.S. v Price* (D NJ 1983) 577 F Supp 1103, 1112. The President's authority under this section has been delegated to the Environmental Protection Agency. 42 USC §9606(c). Similar authority exists under California law for responses to an imminent or substantial endangerment. Health & S C §25358.3(a)(1), (3). Failure to comply with an order from the EPA or Department of Toxic Substances Control (DTSC) may result in fines up to $25,000 per day (42 USC §9606(b)(1); Health & S C §25359.2) and punitive damages in an amount equal to at least three times the cost of cleanup (42 USC §9607(c)(3); Health & S C §25359(a)).

A private party in compliance with a DTSC remediation agreement or order may pursue contribution and treble damages from a private party who is subject to the agreement or order and has not complied. Health & S C §25359.4.5.

Cleanup orders under 42 USC §9613 have generally survived constitutional challenges (see *U.S. v Conservation Chem. Co.* (D Mo 1985) 619 F Supp 162), and the courts have rejected due process challenges to "section 106 orders." See *Wagner Seed Co. v Daggett* (ED NY 1986) 1986 US Dist Lexis 30030, aff'd (2d Cir 1986) 800 F2d 310; *U.S. v Reilly Tar & Chem. Co.* (D Minn 1985) 606 F Supp 412. In *General Elec. Co. v EPA* (DC Cir 2004) 360 F3d 188, there was a facial due process constitutional challenge to CERCLA §105 orders in general (42 USC §§9606, 9613) as opposed to a challenge to a specific EPA order or action. The court held that a constitutional challenge is supported by 42 USC §9613.

California cities and redevelopment agencies also have authority to issue cleanup orders and recover costs from private parties. Redevelopment agencies derive such authority from the Polanco Redevelopment Act (Health & S C §§33459-33459.8). See *Redevelopment Agency v Salvation Army* (2002) 103 CA4th 755, 127 CR2d 30 (redevelopment agency need not comply with CERCLA to recover from former property owner costs of removing contaminated soil from property); see also Brown & Winters, *The Polanco Redevelopment Act: California's Most Important Brownfields Statute*, 26 CEB Real Prop L Rep 174 (Sept. 2003). The Fourth District Court of Appeal has held that a redevelopment agency can sue private parties for injunctive relief under the Polanco Act, and that the agency does not need to show that an "imminent and substantial endangerment" exists or that it incurred any costs or suffered injury. *Redevelopment Agency v San Diego Gas & Elec. Co.* (2003) 111 CA4th 912, 4 CR3d 317. California law also authorizes cleanup orders by cities. Health & S C §§25401-25402.3. However, cities are preempted from using their ordinances to address sites listed by the Department of Toxic Substances Control. *City of Lodi v Randtron* (2004) 118 CA4th 337, 13 CR3d 107.

Only the government, however, has the authority to issue remediation orders. Under CERCLA, a private party cannot require a prior owner who caused contamination on the property to remediate it and is limited to an action to recover costs actually incurred. *Cadillac Fairview/Cal. v Dow Chem. Co.* (9th Cir 1988) 840 F2d 691, 696; *New York v Shore Realty Corp.* (2d Cir 1985) 759 F2d 1032, 1048. Under the Resource Conservation and Recovery Act of 1976 (RCRA) (42 USC §§6901-6992k), however, a private party can obtain an injunction requiring investigation and cleanup. *Lincoln Props. v Higgins* (ED Cal 1993) 1993 US Dist Lexis 1251. See also 42 USC §6972(a). As a practical matter, however, cost recovery actions (see §7.16) are often used by owners who have incurred some response costs as leverage to force a responsible party to agree to take over the remediation in settlement of the action.

© The Regents of the University of California

§7.16 3. Cost Recovery and Contribution

Federal and state statutes permit a party who incurs remediation or removal costs (including the federal or state government) to seek cost recovery from the responsible parties. 42 USC §9607(a)(4)(A)-(B); Health & S C §§25360, 25363(e). Such actions may proceed whether or not the party initiating the action incurred its response costs under a government remediation order, but a plaintiff seeking to recover costs under CERCLA must demonstrate that the response costs were incurred in a manner consistent with the National Contingency Plan (NCP). 42 USC §9607(a)(4)(B). *Carson Harbor Village, Ltd. v Unocal Corp.* (9th Cir 2001) 270 F3d 863; *Cadillac Fairview/Cal. v Dow Chem. Co.* (9th Cir 1988) 840 F2d 691. The NCP in 40 CFR pt 300, required under 42 USC §9605, sets forth the government's cleanup process guidelines. Among other things, the NCP requires parties embarking on a cleanup to provide a meaningful opportunity for public comment on the proposed remediation plan. See 40 CFR §300.430(c). Failure to accommodate such participation has been held to bar the recovery of response costs. *Carson Harbor Village, Ltd. v Unocal Corp., supra*. An owner who acquires contaminated property may recover from its seller or from any other prior owner, if the seller or prior owner owned the property "at the time of disposal of any hazardous substances." 42 USC §9607(a)(2); *Tanglewood E. Homeowners v Charles-Thomas, Inc.* (5th Cir 1988) 849 F2d 1568, 1573. A buyer who later becomes a seller can also become subject to the same exposures from its buyers.

© The Regents of the University of California

§7.17 a. Parties Eligible for Cost Recovery Actions

For many years, only parties who were not potentially responsible parties (PRPs) themselves could bring cost recovery actions under CERCLA §107 (42 USC §9607) and seek joint and several liability. See *Pinal Creek Group v Newmont Mining Corp.* (9th Cir 1997) 118 F3d 1298 (party partly responsible for hazardous waste site was entitled to seek contribution under CERCLA from other PRPs, but such contribution was limited to several liability, not joint liability). In 2007, however, the Supreme Court ruled that a PRP may bring a cost recovery action under §107(a)(4)(B) (42 USC §9607(a)(4)(B)) against other PRPs *and* that those PRPs so sued are themselves able to bring a contribution claim against other responsible parties under CERCLA §113(f) (42 USC §9613(f)). *U.S. v Atlantic Research Corp.* (2007) 551 US 128, 168 L Ed 2d 28, 127 S Ct 2331. A PRP who has not been subject to a §107 cost recovery action is not entitled to seek contribution under §113 but may proceed under §107 for cost recovery. *Kotrous v Goss-Jewett Co.* (9th Cir 2008) 523 F3d 924, 934.

The Supreme Court has ruled that PRPs seeking costs under the CERCLA contribution provision (CERCLA §113; 42 USC §9613) may not proceed with such an action unless (1) the claim has been brought "during or following" a civil action under CERCLA §106 or §107 (42 USC §9613(f)(1)), *or* (2) the plaintiff has resolved its liability to the state or the United States "in an administratively or judicially approved settlement" (42 USC §9613(f)(3)(B)). *Cooper Indus. v Aviall Servs., Inc.* (2004) 543 US 157, 160 L Ed 2d 548, 560, 125 S Ct 577.

It is unclear whether a PRP who cannot meet the eligibility requirements for a contribution action under §113 may pursue a contribution claim under §107. The Supreme Court has expressly left unaddressed the question of whether "§107(a) contains an additional implied right to contribution for PRPs who are not eligible for relief under §113(f)," but suggested the answer would be no. *U.S. v Atlantic Research Corp.* (2007) 551 US 128, 168 L Ed 2d 28, 41 n8, 127 S Ct 2331.

California's Superfund law, the Carpenter-Presley-Tanner Hazardous Substance Account Act (HSA) (Health & S C §§25300-25395.45), does not have restrictive eligibility language like CERCLA §113; it allows any person who has incurred costs in accordance with the HSA to seek contribution. Health & S C §25363(e). Thus, a party's ability to bring a contribution action under the HSA is not affected by *Cooper Indus. v Aviall Servs., Inc., supra*.

© The Regents of the University of California

§7.18 b. Liability and Damages Issues

Although an owner who remediates can pursue an action under cost recovery provisions, recovery actions are often expensive and may not have the desired results. The seller may try to defend the action by claiming that response costs were not incurred in accordance with the National Contingency Plan (42 USC §9607(a)(4)(B); *Cadillac Fairview/Cal. v Dow Chem. Co.* (9th Cir 1988) 840 F2d 691, 695) or may try to minimize its liability by alleging that the buyer either contributed to the problem in some way (see *Chemical Waste Mgmt., Inc. v Armstrong World Indus.* (ED Pa 1987) 669 F Supp 1285) or partially benefited from the remediation it performed. In such cases, a potentially responsible party (PRP) may still be able to assert contribution claims against another PRP under 42 USC §9613(f); it may not, however, claim joint and several liability under 42 USC §9607(a) unless it proves it is an innocent landowner under CERCLA. *Boyce v Bumb* (ND Cal 1996) 944 F Supp 807. See §7.12.

A party that incurs response costs under a remediation order may also be entitled to recovery from the federal Superfund if the claimant can prove by a preponderance of the evidence either that it is not liable for response costs under 42 USC §9607 or that the remediation order was arbitrary or capricious. 42 USC §9606(b)(2). Most parties cannot make either showing. The California statutory scheme provides few recovery rights from the state Superfund and requires the property involved to be an owner-occupied, single-family residence. Health & S C §25375(a)(3)(A).

© The Regents of the University of California

§7.19 c. Attorney Fees

A private litigant's attorney fees in a CERCLA recovery action (42 USC §9607(a)(4)(B)) are not generally recoverable as response costs. *Key Tronic Corp. v U.S.* (1994) 511 US 809, 128 L Ed 2d 797, 114 S Ct 1960. Only fees for services performed by the attorney for work "that is closely tied to the actual clean up" may be response costs covered by CERCLA. 511 US at 820, 128 L Ed 2d at 807. Under 42 USC §9607(a)(4)(A), however, the government can recover its reasonable attorney fees as a part of its response costs. *U.S. v Chapman* (9th Cir 1998) 146 F3d 1166.

A private party may recover attorney fees in an action for injunctive relief under the Resource Conservation and Recovery Act of 1976 (RCRA), but under that statute a plaintiff must show that the hazardous waste "may present an imminent and substantial endangerment." 42 USC §6972(a)(1)(B), (e). Cleanup costs, however, cannot be recovered under the RCRA. In *Meghrig v KFC W., Inc.* (1996) 516 US 479, 134 L Ed 2d 121, 116 S Ct 1251, the Supreme Court held that the RCRA did not authorize a private cause of action to recover environmental costs for the cleanup of toxic waste that does not continue to endanger health or environment at the time of suit. Noting that the citizen-suit provision of 42 USC §6972 is not intended to provide compensation for past cleanup efforts, the Court held that for that provision to become effective there must be "imminent and substantial endangerment to health or the environment" at the time the suit is brought. 516 US at 484, 134 L Ed 2d at 127.

© The Regents of the University of California

§7.20 d. Common Law Actions

Common law actions for nuisance and trespass may be available to a current owner seeking recovery or contribution. See *Meghrig v KFC W., Inc.* (1996) 516 US 479, 134 L Ed 2d 121, 116 S Ct 1251. See also *Chevron U.S.A. Inc. v Superior Court* (1994) 44 CA4th 1009, 54 CR2d 324 (property owner's nuisance and trespass claim for environmental remediation costs against fuel tank installer). There is, however, a 3-year limitations period for commencing an action for trespass and other injuries to real property (CCP §338(b)), which is often a significant hurdle for plaintiffs in recovery actions. A plaintiff can maintain an action for a "continuing" trespass or nuisance, but must demonstrate that the environmental harm is abatable and that the cost of abatement is reasonable. *Mangini v Aerojet-Gen. Corp.* (1996) 12 C4th 1087, 51 CR2d 272. Regarding diminution in the value of contaminated property, the courts have held that such damage can be recovered only as a consequence of a permanent trespass or nuisance. *FDIC v Jackson-Shaw Partners No. 46, Ltd*. (ND Cal 1994) 850 F Supp 839, 842; see also *CAMSI IV v Hunter Tech. Corp.* (1991) 230 CA3d 1525, 282 CR 80; *Mangini v Aerojet-Gen. Corp.* (1991) 230 CA3d 1125, 281 CR 827.

CERCLA establishes a discovery rule in cases brought under state law for personal injury or property damage caused or contributed to by exposure to any hazardous substance. If the applicable state limitations period for such action provides an earlier commencement date than the federally required commencement date, the more lenient federal commencement date will apply. 42 USC §9658(a). The federally required commencement date is the date a plaintiff knew or reasonably should have known that the property damages were caused or contributed to by the hazardous substances concerned. 42 USC §9658(b)(4)(A). See *O'Connor v Boeing N. Am., Inc.* (9th Cir 2002) 311 F3d 1139; *California v Montrose Chem. Corp.* (9th Cir 1997) 104 F3d 1507.

© The Regents of the University of California

§7.21 4. Private Agreement Limitations

Although parties to a transaction can allocate liabilities for remediation costs between themselves (*e.g.,* a seller might indemnify a buyer for preexisting conditions), such allocations are, at least in the Ninth Circuit and California, ineffective against the federal or state government or against third parties bringing actions under 42 USC §9607(a)(4)(B). 42 USC §9607(e); Health & S C §25364. Both statutes provide, in effect, that no indemnification, hold-harmless, conveyance, or similar agreement is effective to transfer liability under the respective statutory schemes from one party to another, even though neither statute was intended to bar the effectiveness of such agreements between the parties. The cases addressing the statutory limitations are discussed further in §7.61.

Ironically, although third parties are not bound by an agreement between two parties to allocate cleanup costs, at least one court has held that such an agreement may constitute a waiver of rights against third parties. In *Southdown v Allen* (ND Ala 2000) 119 F Supp 2d 1223, 1241, the court said that the seller's agreement with the buyer to clean up the site "at the seller's sole expense" waived the seller's CERCLA contribution rights against third parties because the agreement was silent on the issue. Thus, parties should include language preserving contribution rights if they wish to ensure that they retain them.

Landlords and lessees typically agree on allocation of costs and liabilities for environmental problems. Although such agreements are generally upheld, a provision requiring a lessee to clean up "any" contamination might not be enforced, depending on a variety of factors (including the length of the lease term, the cost of complete cleanup and its relationship to the rental cost, and the parties' expectations). *SDC/Pullman Partners v Tolo Inc.* (1997) 60 CA4th 37, 70 CR2d 62 (toxic substance clause in lease did not require lessee to spend potentially enormous sums to extract de minimis amounts of certain molecules to avoid purely speculative environmental liability).

© The Regents of the University of California

§7.22 5. CERCLA Defenses

Four defense provisions of CERCLA are usually relevant to purchase and sale transactions. These are the third party defense (see §7.23), the "innocent landowner" defense (see §7.24), the "contiguous property owner" defense (see §7.30), and the "bona fide prospective purchaser" defense (see §7.31).

The difference between the third party defense and the others is that a third party defense depends on establishing that no "contractual relationship" existed with the defendant landowner (or other potentially responsible party), while the innocent landowner and the bona fide prospective purchaser defenses are used when a contractual relationship exists but is legally negated by the innocent landowner provisions of 42 USC §§9607(b)(3) and 9601(35).

The contiguous property owner and bona fide prospective purchaser defenses are actually variations of the innocent landowner defense that were created as part of the 2002 amendment of CERCLA by the Small Business Liability Relief and Brownfields Revitalization Act (Pub L 107-118, 115 Stat 2356, 2368). In California, the third party and the innocent landowner defenses are incorporated into the Carpenter-Presley-Tanner Hazardous Substance Account Act (HSA) (Health & S C §§25300-25395.45) (see §7.9) under Health & S C §25323.5(b); but rather than amending that Act to include the new federal defenses, the legislature included them in a separate statute, the California Land Reuse and Revitalization Act of 2004 (Health & S C §§25395.60-25395.119) (also known as AB 389). Health & S C §§25395.69, 25395.70. See §7.32.

The so-called secured creditors exemption can also be important to a purchase and sale transaction, but because it is generally more relevant to lender considerations it is covered in §7.88, discussing lender concerns.

Defenses also exist for someone who acquires property by inheritance or bequest (42 USC §9601(35)(A)(iii)); and, theoretically, for contamination caused by acts of God or war (42 USC §9607(b)(1)-(2)), but in practice such defenses almost always fail.

The Ninth Circuit has held that only statutory defenses are available in CERCLA actions; equitable defenses, such as laches, are not available. *California v Neville Chem. Co.* (9th Cir 2004) 358 F3d 661.

© The Regents of the University of California

§7.23 a. The Third Party Defense

Under 42 USC §9607(b)(3), the third party defense is available when a third party:

- Caused contamination by its act or omission;
- Is not an employee or agent of a landowner or another potentially responsible party (PRP); and
- Did not act or fail to act in connection with a contractual relationship (direct or indirect) with the landowner or other PRP.

The landowner or other PRP must also show that "(a) he exercised due care with respect to the hazardous substance concerned… and (b) he took precautions against foreseeable acts or omissions of any such third party and the consequences that could foreseeably result from such acts or omissions." 42 USC §9607(b)(3). For purposes of the third party defense, contractual relationships are defined as including "land contracts, deeds, easements, leases, or other instruments transferring title or possession." 42 USC §9601(35)(A). Contractual relationships have been found with purchasers who failed to achieve innocent landowner status (*U.S. v Pacific Hide & Fur Depot, Inc.* (D Idaho 1989) 716 F Supp 1341, 1347) and lessors (*U.S. v Monsanto Co.* (4th Cir 1988) 858 F2d 160, 169); indirect contractual relationships have been found with sublessees (*Washington v Time Oil Co.* (WD Wash 1988) 687 F Supp 529, 533). Obviously, the third party defense is available only in limited circumstances.

EXAMPLE: In *Monsanto,* the court noted that if the defendants had shown that they removed all their waste from the disposal facility, they might have been able to successfully assert a third party defense. See *U.S. v Monsanto Co.* (4th Cir 1988) 858 F2d 160, 171 n21.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/7 Hazardous Waste Considerations/§7.24 b. The Innocent Landowner Defense

§7.24 b. The Innocent Landowner Defense

The innocent landowner defense under CERCLA is found in 42 USC §9601(35), which excludes from the term "contractual relationship" any relationship in which the "defendant" acquired its property after it was contaminated and did not know and had no reason to know of the contamination when it acquired the property. 42 USC §9601(35)(A). The criteria for the innocent landowner defense are defined as follows (42 USC §9601(35)(B)):

> (B) Reason to know.
>
> (i) All appropriate inquiries. To establish that the defendant had no reason to know of the matter described in subparagraph (A)(i), the defendant must demonstrate to a court that—
>
> (I) On or before the date on which the defendant acquired the facility, the defendant carried out *all appropriate inquiries*, as provided in clauses (ii) and (iv), into the previous ownership and uses of the facility in accordance with generally accepted good commercial and customary standards and practices; and
>
> (II) the defendant took reasonable steps to—
>
> (aa) stop any continuing release;
>
> (bb) prevent any threatened future release; and
>
> (cc) prevent or limit any human, environmental, or natural resource exposure to any previously released hazardous substance. [Emphasis added.]

© The Regents of the University of California

§7.25 (1) Requirements to Qualify for Innocent Landowner Status

Because the innocent landowner defense is part of 42 USC §9601(35), a party seeking to use the defense must still meet the other requirements of 42 USC §9607(b)(3). Therefore, to qualify as an innocent landowner, an owner must have:

- Acquired the property after it was contaminated;
- Undertaken "all appropriate inquiries" on or before the date of acquiring the property as required by 42 USC §9601(35);
- Exercised due care with regard to the contamination (presumably after discovering it); and
- If applicable, taken precautions against foreseeable acts or omissions of third parties as required by §9607(b)(3).

Because the terminology of §9601(35)(A) refers to a defendant who acquired the property after the disposal of contamination on the facility, the CERCLA definition of "disposal" and the cases applying that definition as discussed in §7.12 should be relevant to any effort to claim innocent landowner status. One court has held that a landowner who did not cause the initial release of hazardous substances still will not qualify as an "innocent landowner" if that owner actively spreads the contaminated soil (even if the owner did not know the soil was contaminated). *Lewis Operating Corp. v U.S.* (CD Cal 2007) 533 F Supp 2d 1041, 1047.

PRACTICE TIP: For inquiries made before May 31, 1997, the level of inquiry necessary to satisfy §9601(35)(B) is still unclear. In some circumstances, an inquiry may not be necessary at all. *U.S. v Pacific Hide & Fur Depot, Inc.* (D Idaho 1989) 716 F Supp 1341, 1348, citing *U.S. v Serafini* (MD Pa 1988) 706 F Supp 346. What is clear is that the required level of inquiry depends on the circumstances (*U.S. v Pacific Hide & Fur Depot, Inc., supra*) and that, in most cases, some level of inquiry will be required to establish the defense. The *Pacific Hide* court suggested that the appropriate guideline should be that "[c]ommercial transactions are held to the strictest standard; private transactions are given a little more leniency; and inheritances and bequests are treated the most leniently…." *U.S. v Pacific Hide & Fur Depot, Inc., supra*.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/7 Hazardous Waste Considerations/§7.26 (2) Application to Property Purchased Before May 31, 1997

§7.26 (2) Application to Property Purchased Before May 31, 1997

In 2002, CERCLA was amended by the Small Business Liability Relief and Brownfields Revitalization Act (Pub L 107-118, 115 Stat 2356, 2368) to clarify the standards for establishing the innocent landowner defense. For property purchased before May 31, 1997, a court shall take into account these factors:

- The defendant's specialized knowledge or experience, if any;
- The relationship of the purchase price to the uncontaminated value of the property;
- Any commonly known or reasonably ascertainable information about the property;
- The obviousness of the presence or likely presence of contamination at the property; and
- The ability of the defendant to detect the contamination by appropriate inspection. 42 USC §9601(35)(B)(iv)(I).

© The Regents of the University of California

§7.27 (3) Application to Property Purchased Between May 31, 1997, and November 1, 2006

As part of the 2002 CERCLA amendments, Congress directed the Environmental Protection Agency (EPA) to establish "all appropriate inquiries" standards for property purchased on or after May 31, 1997. 42 USC §9601(35)(B)(iv)(II). Until the EPA promulgated the regulations, which became effective November 1, 2006, the procedures of the American Society for Testing and Materials (ASTM) Standard E1527-97 or Standard E1527-00 (entitled "Standard Practice for Environmental Site Assessments: Phase 1 Environmental Site Assessment Process") satisfied the "all appropriate inquiries" requirements. 42 USC §9601(35)(B)(iv)(II); 70 Fed Reg 66069-66113 (2005). To obtain the ASTM Standards, see the ASTM website in the Directory.

© The Regents of the University of California

§7.28 (4) Application to Property Purchased On or After November 1, 2006

In response to the 2002 congressional directive, the EPA issued final regulations that became effective November 1, 2006. See 40 CFR §§312.1-312.31. Any party who claims protection from CERCLA liability as an innocent landowner, a bona fide prospective purchaser, or a contiguous property owner must meet what is commonly known as the "all appropriate inquiries" requirement under 42 USC §9601(35)(B). Parties who receive grants under the EPA's Brownfields Grant program to assess and characterize properties also must make all appropriate inquiries.

All appropriate inquiries must be conducted or updated within 1 year before the date of acquisition of a property. 40 CFR §312.20(a). If all appropriate inquiries are conducted more than 180 days before the acquisition date, certain aspects of the inquiries must be updated. 40 CFR §312.20(b). Many of the inquiry's activities must be conducted by, or under the supervision or responsible charge of, an individual who qualifies as an environmental professional who has met specific requirements for education and experience. 40 CFR §312.10(b). The environmental professional's inquiry must include (40 CFR §312.21):

- Interviews with past and present owners, operators, and occupants (see 40 CFR §312.23);
- Reviews of historical sources of information (see 40 CFR §312.24);
- Reviews of federal, state, tribal, and local government records (see 40 CFR §312.26);
- Visual inspections of the facility and adjoining properties (see 40 CFR §312.27);
- Commonly known or reasonably ascertainable information (see 40 CFR §312.30); and
- An assessment of the degree of obviousness of the presence or likely presence of contamination at the property and the ability to detect the contamination (see 40 CFR §312.31).

Additional inquiries that must be conducted by or for the prospective landowner or grantee include (40 CFR §312.23):

- Searches for environmental cleanup liens (see 40 CFR §312.25);
- Assessments of any specialized knowledge or experience of the prospective landowner (or grantee) (see 40 CFR §312.28);
- An assessment of the relationship of the purchase price to the fair market value of the property, if the property was not contaminated (see 40 CFR §312.29); and
- Commonly known or reasonably ascertainable information (see 40 CFR §312.30).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/7 Hazardous Waste Considerations/§7.29 (5) Comparison of 'All Appropriate Inquiries' Standards

§7.29 (5) Comparison of "All Appropriate Inquiries" Standards

The EPA's "all appropriate inquiries" standard does not differ significantly from the ASTM Standard E1527-05. (This document can be obtained through the ASTM website; see the Directory.) The current EPA regulations include all the main activities that previously were performed as part of environmental due diligence, such as site reconnaissance, records review, interviews, and documentation of recognized environmental conditions. However, the current regulations extend the scope of some of the environmental due diligence activities and require that significant data gaps or uncertainties be documented. Under the current regulations:

- The subject property's current owner or occupants must be interviewed. (ASTM E1527-00 requires only that the environmental professional make a reasonable attempt to conduct such interviews.)
- Past owners and occupants of the subject property must be interviewed if that is necessary to meet the objectives and performance factors. (ASTM E1527-00 requires the environmental professional to inquire about past uses of the subject property when interviewing the current property owner.)
- If the subject property is abandoned, an owner of a neighboring property must be interviewed. (ASTM E1527-00 requires such interviews at the environmental professional's discretion.)
- There is no specification regarding who is responsible for performing record searches, including searches for use limitations and environmental cleanup liens. (ASTM E1527-00 specifies that these record searches are the responsibility of the user and requires that the results be reported to the environmental professional.)
- Tribal and local government records must be examined. (ASTM E1527-00 has no such requirement.)
- Data gaps must be explicitly identified and documented. (ASTM E1527-00 has no such requirement.)
- There are specific documentation requirements if the subject property cannot be visually inspected. (ASTM E1527-00 has no such requirements.)

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/7 Hazardous Waste Considerations/§7.30 c. The Contiguous Property Owner Defense

§7.30 c. The Contiguous Property Owner Defense

The 2002 CERCLA amendments created a new defense for owners whose property lies over contaminated groundwater, if a number of conditions are met. To qualify for the defense, a "contiguous owner" must establish the following eight conditions by a preponderance of the evidence (42 USC §9607(q)):

- The contiguous owner did not cause, contribute to, or consent to the contamination;
- The contiguous owner is not potentially liable, or affiliated with anyone who is, either "through any direct or indirect familial relationship or any contractual, corporate, or financial relationship" (other than one created by a contract for the sale of goods or services), or as a result of a reorganization of a potentially liable business entity;
- The contiguous owner has taken reasonable steps to
- stop any continuing release;
- prevent any threatened future release; and
- prevent or limit human, environmental, or natural resource exposure to any hazardous substance released on or from property owned by that person (this does not require the contiguous owner to conduct groundwater investigations or cleanup, except in accordance with EPA policy of May 24, 1995, concerning owners of property containing contaminated aquifers);
- The contiguous owner has provided "full cooperation, assistance, and access" for cleanup and restoration;
- The contiguous owner is in compliance with any land use restrictions established or relied on for the cleanup, and has not impeded the effectiveness or integrity of any institutional control;
- The contiguous owner is in compliance with any EPA information request or subpoena;
- The contiguous owner has provided "all legally required notices with respect to the discovery or release of hazardous substances" at the property; and
- When the contiguous owner acquired the property, the contiguous owner (1) conducted all appropriate inquiries, and (2) did not know or have reason to know that the property was or could be contaminated by an offsite release.

The contiguous owner defense suffers from the same limitation as the original innocent landowner defense: If contamination was detected before the contiguous owner acquired the property, the defense is not valid. However, the amendments state that a contiguous owner who fails to qualify because contamination was detected can still seek to qualify as a bona fide prospective purchaser under §9601(40) if the person is otherwise described in that section. 42 USC §9607(q)(1)(C). See §7.31.

Those who do qualify as contiguous owners can request two key legal assurances from the EPA: (1) a covenant not to sue, and (2) CERCLA contribution protection. 42 USC §9607(q)(3).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/7 Hazardous Waste Considerations/§7.31 d. The Bona Fide Prospective Purchaser Defense

§7.31 d. The Bona Fide Prospective Purchaser Defense

The 2002 CERCLA amendments created a new defense that (unlike the innocent landowner and contiguous owner defenses) applies even if the contamination was detected. A person, or tenant of a person, who acquires ownership of a facility after January 11, 2002, and establishes the following eight facts by a preponderance of the evidence, is a "bona fide prospective purchaser" (BFPP) and is not liable for contamination (42 USC §9601(40)):

- All disposal of hazardous substances occurred before the BFPP acquired the facility;
- The BFPP is not potentially liable, or affiliated with anyone who is potentially liable, for response costs at a facility through any direct or indirect familial relationship, or through any contractual, corporate, or financial relationship (other than one created by a contract for sale of goods or services), or as a result of a reorganization of a potentially liable business entity;
- The BFPP has taken reasonable steps to
- stop any continuing release,
- prevent any threatened future release, and
- prevent or limit human, environmental, or natural resource exposure to any previously released hazardous substance;
- The BFPP has provided "full cooperation, assistance, and access" for cleanup and restoration;
- The BFPP is in compliance with any land use restrictions established or relied on for the cleanup, and has not impeded the effectiveness or integrity of any institutional control;
- The BFPP is in compliance with any EPA information request or subpoena;
- The BFPP has provided "all legally required notices with respect to the discovery or release of hazardous substances" at the facility; and
- On acquisition of the property, the BFPP conducted all appropriate inquiry.

PRACTICE TIP: The statutory language excusing contiguous owners from conducting groundwater investigations or cleanup (42 USC §9607(q)(1)(D)) is *not* included in the statutory language relating to BFPPs. This creates an argument, of course, that a BFPP *may* be required to take action with respect to groundwater.

© The Regents of the University of California

§7.32 6. California Land Reuse and Revitalization Act of 2004

Under California's "brownfields" statute, the Land Reuse and Revitalization Act of 2004 (Health & S C §§25395.60-25395.109), buyers of contaminated properties in "urban infill areas" can agree to clean up the property and pay state oversight costs and, in return, receive limited liability protections and a right of contribution to pursue liable parties and recover attorney fees. In 2006, the Act was amended to extend those benefits to long-term lessees. The Act provides immunities under certain circumstances at certain sites.

The Act also creates an option for a prospective purchaser of contaminated property (termed a "bona fide purchaser"; see Health & S C §§25395.69, 25395.80; §7.31) to get a preview of what an agency is likely to require for cleanup by entering into a "consultative services agreement" with an agency (*e.g.,* the State Water Resources Control Board, a Regional Water Quality Control Board, or the Department of Toxic Substances Control). See Health & S C §25395.116. The prospective purchaser pays for the agency's services. Health & S C §25395.116(c)(1). The agency is directed to meet to discuss the environmental data and develop plans within 30 days of submission, and then provide comments on (1) what information, if any, might be needed to formulate a cleanup plan; (2) any proposed response actions that may be necessary; and (3) an estimate of the time required to approve a bona fide purchaser agreement. Health & S C §25395.116(c)(3), (d). If the agency declines to enter into a consultative services agreement, it must provide "specific reasons for its decision" to the prospective purchaser; however, the agency's entry into such agreements is "subject to available staff and resources, as determined by the agency." Health & S C §25395.116(d).

© The Regents of the University of California

§7.33 a. Eligible Property

A buyer seeking brownfield status must obtain a determination from the governing agency that the subject property is eligible under the Act. The site cannot be a listed federal or state Superfund site or a petroleum-release-only site eligible for reimbursement under the state Underground Storage Tank Cleanup Fund. Health & S C §25395.79.2(b). The property must be located in both an "urban area" and an "infill area." Health & S C §25395.79.2(a). An "urban area" is defined as an incorporated city, or an unincorporated area "completely surrounded by one or more incorporated cities," in which (1) the unincorporated area, and the surrounding incorporated cities, have populations of 100,000 or more, and (2) the population density of the unincorporated area is at least as great as the density of the surrounding cities. Health & S C §25395.79.2(c)(2). An "infill area" is defined as "a vacant or underutilized lot of land within an urban area that has been previously developed or that is surrounded by parcels that are or have been previously developed." Health & S C §25395.79.2(c)(1).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/7 Hazardous Waste Considerations/§7.34 b. Bona Fide Purchaser

§7.34 b. Bona Fide Purchaser

If the property qualifies, the purchaser must meet all of the qualifications for a "bona fide purchaser" under the California Land Reuse and Revitalization Act of 2004. The qualifications are essentially the same as those required to be a "bona fide prospective purchaser" under CERCLA (42 USC §9601(40)). The contamination must have occurred before the purchaser acquired the site, and the purchaser must not be potentially liable, or affiliated with anyone who is. Health & S C §25395.69(a). In addition, the purchaser must prove "by a preponderance of the evidence" that the purchaser (Health & S C §25395.80):

- Made "all appropriate inquiries" into the previous ownership and uses of the site on or before acquisition;
- Exercised "appropriate care" with respect to the contamination;
- Provided "full cooperation, assistance, and access" to persons authorized to clean up;
- Complied with land use controls relating to a cleanup and did not impede any cleanup;
- Complied with all requests for information from any agency; and
- Provided "all notices and satisfie[d] reporting requirements required by state or federal law with respect to the discovery or release of hazardous substances at the site."

Under Health & S C §29395.64, the purchaser must enter into an agreement with the State Water Resources Control Board, a Regional Water Quality Control Board, or the Department of Toxic Substances Control to:

- Perform a site assessment and, if the agency determines it is necessary, prepare and implement a response plan (Health & S C §29395.92(a));
- Reimburse the agency for all costs (Health & S C §29395.93(b)); and
- Provide notice and opportunity for public participation if a response plan is required (Health & S C §29395.96(a)).

© The Regents of the University of California

§7.35 c. Immunity From Cleanup Costs

The California Land Reuse and Revitalization Act of 2004 (Act) protects bona fide purchasers from nonagency claims for cleanup costs and some other damages under state statutes. Specifically, the participating purchaser "is not liable under any applicable statute for a claim made by any person, other than an agency, for response costs or other damages associated with a release or threatened release of a hazardous material at the site." Health & S C §25395.81(a)(1).

PRACTICE TIP: The legislative counsel's digest for the Act (Stats 2004, ch 705) asserts that it provides immunity from claims "under specified state statutory and common laws"; however, that language is not in the Act itself. The Act defines the phrase "applicable law" to include certain common law actions (see Health & S C §25395.66), but the phrase "applicable law" is *not* used in the section providing liability immunity (Health & S C §25395.81); instead, the phrase "applicable statute" is used. This discrepancy may be a drafting error, but it is not an error that a buyer can assume will be corrected. The phrase "applicable statute" is likely to be interpreted to mean what it says. Thus, the Act likely will *not* insulate a bona fide purchaser from common law claims.

Common law claims represent only one category of claims from which a bona fide purchaser is not protected. Others include the following:

- Claims under federal statutes (such as CERCLA and RCRA) (see Health & S C §§25395.66 ("applicable law" does not include federal statutes), 25395.81 (providing immunities under "state statute"));
- Claims for bodily injury or wrongful death (Health & S C §25395.86(a)(1));
- Claims under the state Hazardous Waste Control Law (Health & S C §25395.86(a)(2));
- Criminal acts and permit violations (Health & S C §25395.86(a)(3)-(4));
- Claims by a redevelopment agency under the Polanco Act (Health & S C §25395.86(b)); and
- Claims by the State Water Resources Control Board, a Regional Water Quality Control Board, or the Department of Toxic Substances Control that are "necessary to protect public health and safety or the environment pursuant to an applicable statute" (Health & S C §25395.86(c)).

The Act explicitly provides the participating purchaser with a right of contribution (Health & S C §25395.85), including attorney fees and experts' fees, if the purchaser prevails and had served a written demand (which does *not* include attorney fees or experts' fees) for cleanup costs at least 20 calendar days before trial. Health & S C §25395.84.

NOTE: There is a potential hurdle in seeking to exercise a right of contribution. The Seventh Circuit has held that cleanup costs are *not* recoverable under a state contribution statute unless they are consistent with the National Contingency Plan (NCP), the EPA's cleanup process regulations. *PMC, Inc. v Sherwin-Williams Co.* (7th Cir 1998) 151 F3d 610, 617. The court reasoned that Congress created a sanction in CERCLA by prohibiting private parties from recovering cleanup costs inconsistent with the NCP, and that a private party cannot nullify that sanction by recovering costs under a general state contribution statute. Whether courts in the Ninth Circuit will accept or reject (or perhaps distinguish) the *PMC* decision remains to be seen.

The Act also allows an agency to file a lien on the property for any "unrecovered costs" in an amount not to exceed (1) the increase in fair market value attributable to the cleanup at the time of the property's disposition, and (2) the unrecovered response costs actually incurred by the agency. Health & S C §25395.83.

© The Regents of the University of California

D. Investigation and Review of Environmental Conditions

§7.36 1. California Toxic Disclosure Statutes

The due diligence process for toxic contamination in California has been made somewhat easier by California's statutory disclosure requirements. Two sets of statutes basically require sellers of residential and commercial real properties to disclose known toxic contamination to buyers and, in certain circumstances, other third parties.

Under Health & S C §25359.7(a), an owner of nonresidential real property must disclose releases of hazardous substances located on or beneath the property to purchasers, lessees, or renters of the property when the owner either knows of such a release or has reasonable cause to believe that it has occurred. (Section 25359.7(b) requires lessees to make the same disclosures to owners or lessors.) A seller or lessee who breaches this disclosure obligation will be

- responsible for actual damages;
- potentially liable for a civil penalty of $5000 for each violation; and
- subject to any other remedies that may be provided by law.

Sellers of residential real property must comply with CC §§1102-1102.17, which establish an obligation for disclosures and a statutory disclosure form for residential real property transfers. The statutory form (see §6.37) specifically requires the seller to answer the following question (CC §1102.6):

> II. SELLER'S INFORMATION
> …
> C. Are you (Seller) aware of any of the following:
> 1. Substances, materials, or products which may be an environmental hazard such as, but not limited to, asbestos, formaldehyde, radon gas, lead-based paint, mold, fuel or chemical storage tanks, and contaminated soil or water on the subject property. ___ Yes ___ No

In short, any seller of real property in California must disclose the existence of toxic contaminants of which it is aware, and for nonresidential property a disclosure is also required if the seller has reasonable cause to believe that contamination may exist. See §§7.46-7.52 for discussion of the provisions the parties might include in an agreement to address the fact that no contamination is known to exist or that known contamination has been disclosed.

© The Regents of the University of California

2. Environmental Assessments

§7.37 a. Phase I Reports

Usually, one party in a commercial transaction is likely to obtain a so-called Phase I Environmental Report (Phase I Report). In most larger commercial transactions, the lender will require a Phase I Report, but in smaller commercial transactions or residential purchases it will be the parties' decision (usually the buyer's), based on the available information about the property and surrounding area and the desired level of protection. The buyer's counsel should consult with the buyer on the need for a Phase I investigation and the risks of failing to make such an investigation.

Phase I Reports sometimes go by other names, including "preliminary site assessments" and "environmental site surveys." Most site assessments follow the protocol set out in American Society for Testing and Materials (ASTM) Standard E1527-05 ("Standard Practice for Environmental Site Assessments: Phase I Environmental Site Assessment Process"; see the Directory for the ASTM website, which provides a summary of this document and instructions on how to order it). The ASTM has revised its standards to incorporate the EPA's regulations regarding "all appropriate inquiries." See §§7.53-7.54.

A Phase I Report normally includes the following:

- A review of various lists maintained by the EPA, Regional Water Quality Control Board (RWQCB), the Department of Health Services (DHS), and others identifying properties known to have been affected by toxic contamination;
- Discussions, if possible, with various agency representatives to ascertain whether a site is known or believed to have been affected by toxic contamination but is not yet on the relevant lists;
- Review of the historical uses of the site by interviewing surrounding property owners, reviewing historical aerial photos, and reviewing historical title chains (if title chains are provided to the consultant or ordered by the consultant for an additional fee); and
- A site inspection by the consultant to ascertain whether any signs of contamination are visible at the property itself.

It is sometimes appropriate to provide historical title chains to consultants for their review. Title chain reviews that identify previous owners of record, including lessees or lenders, are available from most title companies, and may indicate the past uses of the property.

The reviews usually focus on the property that is the subject of the report and on surrounding properties for a distance of a quarter mile to one mile, depending on the extent of nearby development. Surrounding properties are reviewed to enable the consultant to identify potential offsite sources of toxic contamination.

EXAMPLE: Disclosure of groundwater contamination on adjacent property might lead the consultant to recommend that groundwater samples be collected and tested from the property to be acquired, unless the owner of the contaminated property has already identified the perimeter of the contamination.

On chain of title guaranties, see California Title Insurance Practice §9.18 (2d ed Cal CEB 1997). On the role of recorded document guaranties in environmental due diligence, see Title Ins §§9.16-9.17.

Some buyers request a modified Phase I Report in which the consultant is asked to undertake asbestos samplings concurrently with its site inspection. A normal Phase I investigation merely identifies potential asbestos-containing materials (ACMs), while taking samples of the potential ACMs is deferred to a Phase II investigation.

© The Regents of the University of California

§7.38 b. Phase II Reports

When the parties are aware of toxic contamination that affects or has a significant potential to affect the property, the buyer will likely require a Phase II Report, which typically involves the collection and analysis of samples of soil, groundwater, or both. Phase II Reports are often done in stages, in which a few samples are taken initially and further samples are taken if contamination is shown.

The focus of a Phase II investigation first should be to confirm whether the potential contamination disclosed by the Phase I Report or by the seller actually exists. If it does, the next step is to ascertain the types of contaminants present, whether they exist in quantities that will require them to be reported or remediated (sometimes referred to as threshold quantities or action levels), and the approximate quantity of contamination to be remediated.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/7 Hazardous Waste Considerations/§7.39 c. Remedial Investigation/Feasibility Study/Remedial Action Plan

§7.39 c. Remedial Investigation/Feasibility Study/Remedial Action Plan

Before proceeding with remediation, most owners require preparation—and, if applicable, governmental approval—of a remedial investigation report, a feasibility study (assessing various cleanup options), and a remedial action plan. The costs of remediation usually cannot be reliably estimated until the plan is completed, but if the contamination identified for removal in preceding reports can be quantified, that information may be useful for preliminary cost estimates. Remediation plans often include land use restrictions, which are recorded and run with the land. CC §1471.

EXAMPLE: A modified Phase I Report that includes asbestos sampling should include sufficient information on the quantity of asbestos-containing materials to permit a fairly reliable estimate. In contrast, it is unlikely that any reliable cost estimate for groundwater remediation will be possible before a remedial action plan is completed.

© The Regents of the University of California

§7.40 3. Seller's Review of Property

It is generally preferable for a seller to be aware of toxic contamination affecting its property before entering into an agreement to sell it, especially if the seller has reason to believe that contamination may exist that would have to be disclosed under Health & S C §25359.7(a). See §7.36. If the seller does not disclose the existence of possible contamination and the buyer's consultant identifies the potential for toxic contamination in a Phase I Report, the buyer will typically disapprove of the physical condition of the property under normal due diligence provisions of the agreement. See §§7.53-7.59. The buyer will then decide whether it is still interested in acquiring the property in light of the contamination. If the buyer decides to proceed, a further delay will occur until the parties agree on the manner in which the contamination will be remediated or removed, which party will be responsible, and any appropriate price adjustments. See §7.60. If the buyer decides not to buy the property, the seller will have lost substantial time and money in marketing, negotiating, and documenting a transaction that will not occur.

Alternatively, if the seller initiates an investigation before marketing the property, it will be able to either inform a buyer that the property is free of contamination or address and negotiate the steps that must be taken to remediate the contamination. The seller may then be able to market the property while simultaneously undertaking Phase II investigations or having a remediation plan prepared and approved. When the seller later finds a buyer for the property, it can disclose what is known about the contamination and what will be done about it and, possibly, have an approved remediation plan that can become a part of the purchase and sale agreement. The agreement will then clearly outline each party's rights and responsibilities on any required remediation and the time frames for performance.

The risk of performing studies in advance, however, is that the seller may have to disclose problems that are found to a potential buyer or a governmental agency, or begin remediation sooner than desired. To avoid this risk, many sellers avoid obtaining a Phase I Report until the buyer is identified and an agreement signed. Other sellers defer a Phase I Report in order to try to shift the cost of preparing the report to the buyer as part of its due diligence costs.

© The Regents of the University of California

§7.41 4. Buyer's Review of Property

Most buyers will wish to have their consultant prepare a Phase I Report unless they have already been given one by the seller. To qualify for CERCLA's defenses, a prospective buyer must complete a Phase I Report that is consistent with EPA's regulations requiring "all appropriate inquiries." See §§7.22-7.31. See also the discussion in §§7.53-7.54 of the buyer's due diligence provisions. In reviewing a Phase I Report supplied by the seller or prepared for the buyer, the buyer should focus on matters that would affect, or potentially affect, the use or development of the subject property, as well as on potential liability issues.

A parcel of land that is designated as hazardous waste property or as border-zone property under Health & S C §25229 may not be used for certain purposes; for example, a border-zone property, although not itself contaminated, may not be used for residential, hospital, school, or day-care buildings. Health & S C §25232(a)-(b).

Sophisticated buyers may be able to help focus the environmental consultant on issues that would normally be beyond the scope of the Phase I Report, based on their own walk-through at the property.

EXAMPLE: If the buyer has noticed soil discoloration or learned that a gas station was formerly located on the property, then, based on discussions with the local planning department, the consultant can be instructed to take soil or groundwater samples concurrently with the Phase I investigation. The buyer may also wish to instruct the consultant to do asbestos sampling concurrently with the Phase I investigation if the building's age indicates that asbestos-containing materials were likely used in its construction.

If a Phase I Report identifies potential contamination problems, a qualified environmental consultant (see §7.42) is best equipped to advise the buyer of the issues that should be reviewed as part of a Phase II Report.

© The Regents of the University of California

5. Use of Environmental Consultants

§7.42 a. Scope of Work

To obtain the best possible work product from an environmental consultant, it is important to establish a clear scope of work for the consultant to perform at each step of the process. If a full Phase I Report is desired, the consultant's employer should confirm that the consultant's proposal includes all the typical elements of a Phase I Report (as discussed in §7.37) and should review the full report to make sure that all the steps agreed to by the parties were performed. Many parties will request a draft Phase I Report to enable them or their counsel to offer recommendations for the final product. If the work involves Phase II investigations, the employer should be integrally involved in deciding such matters as the number and type of samples to be taken, the location of sampling sites, and whether sampling will be performed on the entire site at once or in phases.

© The Regents of the University of California

§7.43 b. Confidentiality

Property owners usually would like to prevent a consultant or a buyer from disclosing to governmental entities or third parties contamination that it discovers as part of due diligence. Under 42 USC §9603, the legal responsibility for notifying the Environmental Protection Agency of a release lies with the individual in charge of the facility where the release occurred. Thus, a prospective buyer or an environmental consultant need not disclose contamination that it discovers to governmental agencies and can accept a seller's requirement that the parties maintain the confidentiality of the information they find. As with most nondisclosure provisions, the parties may wish to provide in the agreement for permitted disclosures when required by a court or a governmental agency.

© The Regents of the University of California

§7.44 c. Principal-Agent Considerations

Whether the seller or the buyer retains the environmental consultant, the parties should remember that the consultant is the agent of the party that hired it and must take its instructions from that party. As an agent, a consultant can also bind its principal when the agent has actual or, sometimes, apparent authority. This may be important when the consultant is directing remediation activities, hiring contractors, or reporting to governmental agencies on behalf of an owner. In preparing a contract with an environmental consultant, counsel may wish to review CC §§2295-2357, covering agency relationships, as well as provide clear instructions on the scope of the consultant's authority as agent and the consultant's responsibility for liabilities that it may create for its principal.

© The Regents of the University of California

§7.45 II. CONTRACTUAL PROVISIONS ON TOXIC CONTAMINATION

The provisions that parties to a purchase and sale or lease transaction should include in their agreement will depend on the known or expected environmental condition of the property at the time the agreement is signed. Because contamination problems vary greatly and are very complex, the forms used will vary considerably. The provisions used in this chapter are illustrative forms addressing typical situations; they do not address all of the unique situations presented as examples in the text.

Drafting provisions on toxic contamination usually occurs in one of three different situations:

- *No known contamination.* When there is no known toxic contamination, the agreement will usually be limited to provisions (1) containing the seller's representation and warranty that no toxic contamination is known to exist on the property, (2) giving the buyer the right to investigate the environmental condition of the property, and (3) making the buyer's satisfaction with the investigations a condition precedent to the closing. In a larger transaction, the agreement might also include a de minimis clause under which one party takes responsibility for any discovered contamination that will cost less than a fixed dollar amount to remediate.
- *Previously completed Phase I Report.* If the seller has already completed a Phase I Report (defined in §7.37) or other environmental inspection, it should be reviewed by the buyer's counsel and environmental consultant before the buyer executes an agreement. Any problems identified in that report, or any further testing that the report requires or recommends, should be covered in the agreement.
- *Problems discovered after execution of agreement.* Any environmental problems identified as part of the buyer's due diligence and not previously covered in the agreement will probably need to be addressed in one or more amendments to the agreement. See §7.60. Of course, if the parties cannot agree on how to resolve the environmental problems found during the due diligence period, one or both parties will likely terminate the transaction.

© The Regents of the University of California

A. Seller's Documentation of Knowledge

§7.46 1. Disclosure of Knowledge

The seller of real property must disclose any known toxic contamination to the buyer and, for nonresidential property, suspected toxic contamination. Health & S C §25359.7(a); CC §§1102-1102.17. See §7.36.

The seller, to avoid disputes on what has been disclosed, should include its disclosures in the purchase and sale agreement or in a separate writing. If the disclosures are based on an environmental report, the agreement should identify the report by reference or include a copy of it as an exhibit. If the seller has not had a Phase I Report prepared before signing the purchase and sale agreement and does not know of any contamination, the agreement should clearly state which party will be responsible for having the report prepared and should state that both parties are relying on the consultant's investigation.

© The Regents of the University of California

§7.47 2. Representations and Warranties

Most buyers of real property will want some form of representation and warranty from the seller that the property is unaffected by toxic contamination. Representations are negotiable and can cover a range of liability scenarios. Four examples of typical representation and warranty clauses are provided in §§7.49-7.52: an absolute representation (§7.49); a representation made to the best of the seller's actual knowledge (§7.50); and representations limited to specific individuals (§7.51) or specific facts disclosed by a Phase I Report (§7.52). A seller may also choose to make no representations at all.

Though such provisions are unlimited as to time, many sellers try to limit their representations to the period when they owned the property. From a buyer's standpoint, this limitation is undesirable because the buyer risks liability regardless of when the contamination occurred.

Each form in §§7.49-7.52 assumes that the term "hazardous materials" is already defined elsewhere in the agreement. A typical, but simple, definition of hazardous materials appears in §7.48. See §4.173 for form provisions on seller's representations.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/7 Hazardous Waste Considerations/§7.48 a. Form: Definition of 'Hazardous Materials'

§7.48 a. Form: Definition of "Hazardous Materials"

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§7.48-7.80.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

7.48-1 Definition of "hazardous materials"

The term "hazardous materials" when used in this Agreement shall mean any hazardous waste or hazardous substance as defined in any federal, state, or local statute, ordinance, rule, or regulation applicable to the property, including, without limitation, as amended, the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (Title 42 United States Code §§9601-9675), the Resource Conservation and Recovery Act of 1976 (Title 42 United States Code §§6901-6992k), the Carpenter-Presley-Tanner Hazardous Substance Account Act (Health and Safety Code §§25300-25395.45), and the Hazardous Waste Control Law (Health and Safety Code §§25100-25250.28). "Hazardous materials" shall also include asbestos or asbestos-containing materials, radon gas, and petroleum or petroleum fractions, whether or not defined as a hazardous waste or hazardous substance in any such statute, ordinance, rule, or regulation.

Comment: As used in this chapter, the term "hazardous materials" generally conforms to this definition. Some attorneys use a more extensive definition, which may include the federal and state underground storage tank statutes and other federal or state statutes.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/7 Hazardous Waste Considerations/§7.49 b. Form: Absolute Representation

§7.49 b. Form: Absolute Representation

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§7.48-7.80.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

7.49-1 Absolute representation

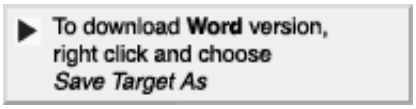
Seller hereby represents and warrants to Buyer that no hazardous materials are located on or under the property; that there has been no release, storage, treatment, generation, or disposal of any hazardous materials on, under, or from the property; and that no hazardous materials have been transported from the property.

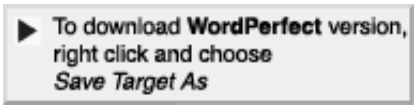
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/7 Hazardous Waste Considerations/§7.50 c. Form: Best of Knowledge

§7.50 c. Form: Best of Knowledge

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§7.48-7.80.





7.50-1 Best of knowledge

Seller hereby represents and warrants to Buyer that to the best of Seller's actual knowledge, and without any independent investigation having been made by Seller, no hazardous materials are located on or under the property; that there has been no release, storage, treatment, generation, or disposal of any hazardous materials on, under, or from the property; and that no hazardous materials have been transported from the property.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/7 Hazardous Waste Considerations/§7.51 d. Form: Best of Knowledge (Specific Individuals)

§7.51 d. Form: Best of Knowledge (Specific Individuals)

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§7.48-7.80.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

7.51-1 Best of knowledge (specific individuals)

Seller hereby represents and warrants to Buyer that to the best actual knowledge of _ _[*names of individuals who work for Seller*]**_ _, and without any independent investigation having been made by Seller, no hazardous materials are located on or under the property; that there has been no release, storage, treatment, generation, or disposal of any hazardous materials on, under, or from the property; and that no hazardous materials have been transported from the property.**

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/7 Hazardous Waste Considerations/§7.52 e. Form: Best of Knowledge With Exception for Phase I Report

§7.52 e. Form: Best of Knowledge With Exception for Phase I Report

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§7.48-7.80.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

7.52-1 Best of knowledge with exception for Phase I Report

Seller hereby represents and warrants that to the best of Seller's knowledge, and except as otherwise disclosed by that certain environmental report dated _ _[*date*]_ _ prepared by _ _[*name of environmental services company*]_ _, a copy of which report is attached as Exhibit _ _ and incorporated in this document by this reference (Environmental Report), that no hazardous materials are located on or under the property; that there has been no release, storage, treatment, generation, or disposal of any hazardous materials on, under, or from the property; and that no hazardous materials have been transported from the property. Buyer understands and acknowledges that Seller has not undertaken any investigation or inspection of the property with regard to environmental matters and that both Seller and Buyer are relying solely on the Environmental Report as the only investigation and inspection undertaken by Seller with regard to these matters.

© The Regents of the University of California

§7.53 B. Buyer's Rights Regarding Unknown Contamination

The agreement should include various provisions that give the buyer an opportunity to investigate the property for contamination and define the buyer's rights as to contamination it may discover. See §4.171 for form provisions on buyer's contingencies. Various statutes require the property owner to report the discovery of contamination to regulatory agencies, so an owner who learns of the buyer's discovery may have reporting obligations (and the buyer may have such obligations after acquisition of the property). See, *e.g.,* Health & S C §§5411.5, 25189, 25359.4, 25359.7(a); Wat C §§13260, 13264, 13271. Most of these provisions will need to be included even if the seller has already disclosed some contamination.

© The Regents of the University of California

§7.54 1. Conditions Precedent for Due Diligence

In addition to a representation and warranty on environmental matters, a buyer usually wants the right to conduct its own review of the environmental condition of the real property and to condition its completion of the purchase on its satisfaction with or waiver of such review.

A seller who has already had a Phase I Report prepared may want the buyer to review the report and waive any contingency related to environmental matters before signing a purchase and sale agreement. Most buyers, however, will still want to have an opportunity after signing the agreement to review the report and perform follow-up testing, if the buyer decides such testing is necessary or appropriate. Even when a Phase I Report prepared for the seller concludes that contamination is unlikely, the buyer should retain its own environmental consultant to review that report either before or after signing the agreement, as applicable, because the report may indicate contamination of nearby properties that the buyer should know about.

If the seller has not prepared a report, the parties will need to negotiate the time period in which the buyer will have the right to complete its Phase I Report or other review and to satisfy or waive its contingency. If a Phase I Report is the only review that must be completed, the typical real property due diligence period of 30 days is usually adequate for most properties. If, however, a previously prepared Phase I Report indicates the need for Phase II investigations, then a 30-day due diligence period will probably not be enough to complete sampling and laboratory testing. Both parties should review the appropriate time frames with their environmental consultants, based on the work anticipated, and then try to agree on the time frame to complete it.

If the buyer plans to undertake more than a Phase I Report, the seller should make sure that the agreement contains appropriate protections intended to ensure that the work will be performed properly and without undue delay. The parties should agree on the scope of the investigation, and the seller should retain the right to require split samples, which it can have separately analyzed to verify the buyer's findings. These provisions should also be a part of any amendment addressing Phase II work after initial due diligence discloses previously unknown contamination. The exact nature of such protective provisions will vary greatly with the nature of the reviews to be undertaken, the relationship between the parties, and each party's knowledge of and comfort with the consultant performing the reviews. Because so many variables affect the drafting of such provisions, a sample form has not been included in this chapter. See §8.68 for a broad form of access provision.

© The Regents of the University of California

§7.55 2. Lessee's Estoppel Provision

If the property to be acquired is leased to one or more third parties, especially if the tenant is using the property for industrial purposes, the buyer will want to include, as an element of the buyer's due diligence process, confirmation that the lessees are not aware of any toxic contamination. Such confirmation would typically take the form of a statement in the estoppel letter to be obtained from the lessees, before closing, to the effect that: "Lessee is not aware of the existence, storage, treatment, release, or disposal of any hazardous materials on, under, or from the property except as set forth below." For a form definition of "hazardous materials," see §7.48. The disclosure of contamination by a tenant should permit the buyer to withdraw from the transaction or otherwise address the issue. See also §7.41 for discussion of the buyer's review of the property. The buyer or its counsel should also review any leases affecting the property and verify that they require contamination caused by the lessee or lessees to be remediated or removed.

© The Regents of the University of California

§7.56 3. Seller's De Minimis Obligation to Remediate

In larger transactions, buyers and sellers will sometimes seek to obligate one party or the other, usually the seller, to remediate or remove all toxic contamination found on the property as a result of the buyer's due diligence, to the extent that the cost of remediating or removing it does not exceed a fixed dollar amount. If the agreement includes such an obligation, it will be beneficial for the parties to similarly address the various other provisions outlined in this chapter to ensure that the agreement reflects the entire agreement intended by the parties. For a typical provision requiring the seller to remediate de minimis contamination, see form 7.57-1.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/7 Hazardous Waste Considerations/§7.57 4. Form: Seller to Remediate De Minimis Contamination

§7.57 4. Form: Seller to Remediate De Minimis Contamination

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§7.48-7.80.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

7.57-1 Seller to remediate de minimis contamination

If Buyer identifies hazardous materials on or under the property during the due diligence period, Seller shall be obligated to diligently cause the remediation or removal of such hazardous materials before the close of escrow, as long as they can be remediated or removed in _ _[*e.g., 120*]_ _ days or less, and as long as the cost of this remediation or removal does not exceed _ _[*e.g., $50,000*]_ _. If Seller is required to remediate or remove hazardous materials under this section, the closing date shall be extended by _ _[*e.g., 120*]_ _ days or such lesser period as Seller requires to complete the remediation or removal, including preparing a work plan for the remediation or removal and obtaining all necessary governmental approvals for the work. Despite any contrary provisions, Seller shall have no remediation or removal obligations under this agreement, may cease any remediation or removal efforts previously commenced, and may terminate this agreement if: (a) the identified hazardous materials cannot be remediated or removed without the removal or demolition of any portion of the improvements on the property; (b) the remediation or removal cannot actually be completed within _ _[*e.g., 120*]_ _ days despite Seller's diligent efforts to do so; or (c) the actual cost of remediation or removal, or the actual costs incurred plus the estimated costs to complete the remediation or removal at any time prior to completion of the same, exceeds _ _[*e.g., $50,000*]_ _. If Seller proceeds to commence remediation or removal of the identified hazardous materials but cannot complete the remediation or removal within _ _[*e.g., 120*]_ _ days, Seller may, at its option, extend the closing date for an additional period of up to _ _[*e.g., 60*]_ _ days to enable it to complete the remediation or removal before close of escrow. As long as Seller completes the remediation or removal of the identified hazardous materials under this section, Buyer shall have no right to terminate this agreement on account of its discovery of hazardous materials. If Seller elects to terminate the agreement under this section, Buyer shall have the right, within _ _[*e.g., 10*]_ _ days after receipt of Seller's notice of termination, to waive Seller's obligations under this section and accept the property in its then current condition as long as: (a) Buyer provides Seller with assurances reasonably satisfactory to Seller that Buyer will complete the remediation of the identified hazardous materials diligently after closing; and (b) Buyer releases Seller from any liability or obligations with regard to the identified hazardous materials and their remediation or removal.

Comment: An alternative de minimis clause that some parties use requires the buyer to accept the property despite the discovery of toxic contamination if the estimated cost of remediation does not exceed a maximum amount. However, given the uncertainty of remediation cost estimates, the continuing nature of environmental liability, and the fact that ownership of any contaminated soils, materials, or, in some cases, groundwater, remains with the party that disposes of it (see §§7.10-7.16), most buyers prefer to avoid such alternative provisions.

© The Regents of the University of California

§7.58 5. Rights to Terminate

Without a de minimis clause (see §§7.56-7.57), a buyer typically has the right to terminate a transaction if toxic contamination is found as part of the buyer's due diligence. In the purchase and sale agreement, the right to terminate would normally be included in the provision that makes the buyer's review and approval of the condition of the property, including environmental matters, a contingency to closing. See discussion in §4.99. See §4.171 for form provisions on buyer's contingencies, and specifically sections 3.1.14 and 3.5 in form 4.171-5.

Like the buyer, the seller may also want to have the right to terminate the agreement because of environmental concerns, unless the agreement includes other provisions addressing the parties' rights and obligations regarding the identified toxic contamination. See §§7.61-7.72. Even if the seller is released and indemnified by a buyer, the seller of contaminated property (depending on the seller's activities on the property) may have continuing liability to the government or third parties for remediation costs as a prior owner. 42 USC §9607(e); Health & S C §25364; see §7.21. Accordingly, it is in the seller's best interests to ensure that the remediation is handled properly. Without assurances that the buyer would properly and expeditiously complete remediation, the seller may wish to terminate its agreement with the buyer and complete the work itself.

© The Regents of the University of California

§7.59 6. Loan Contingency Relationship

In the course of negotiating the environmental due diligence and condition precedent provisions, the parties must also keep in mind that the buyer's lender will likely require a Phase I Report showing that the property is free of environmental problems. Any contingencies in the buyer's favor will need to be drafted with due regard for lender requirements and time frames.

© The Regents of the University of California

§7.60 C. Renegotiation of Price or Other Terms When Undisclosed Toxics Are Found

If the buyer discovers previously undisclosed toxic contamination during its due diligence period, various provisions of the purchase and sale agreement will likely need to be amended if the parties wish to proceed with the transaction. Such provisions might include the following:

- The purchase price; the closing date; release clauses (see §§7.61-7.65);
- Indemnification provisions (see §§7.66-7.72);
- Allocation of the costs of, responsibility for, and control over the remediation process (see §§7.73-7.76); and
- Escrow holdbacks and other measures to secure payment of the remediation costs by seller or buyer as protection for the other party (see §§7.78-7.83).

The parties and their counsel will need to negotiate the various issues. Foremost among others, the parties must decide whether the buyer will (1) purchase the property without a price adjustment if the seller remediates the discovered contamination; or (2) for an appropriate price adjustment, either accept the property in its contaminated state or agree to remediate after closing. For further discussion, see §7.74. After that initial negotiation is completed, the general features of most of the remaining provisions discussed in §§7.61-7.83 will fall into place.

© The Regents of the University of California

§7.61 D. Release Clauses

A buyer and seller may agree between themselves that one will release the other from liability under CERCLA and the HSA (the Carpenter-Presley-Tanner Hazardous Substance Account Act (Health & S C §§25300-25395.45)); however, such agreements will not relieve the released party from liability to the government or to third parties making a claim under 42 USC §9607. 42 USC §9607(e); Health & S C §25364; *Mardan Corp. v C.G.C. Music, Ltd.* (9th Cir 1986) 804 F2d 1454, 1458. See also *Niecko v Emro Mktg. Co.* (ED Mich 1991) 769 F Supp 973, 987. The extent to which any particular release provision is effective will be a state law issue. *Mardan Corp. v C.G.C. Music, Ltd., supra*.

Both CERCLA and the HSA provide that no indemnity, hold harmless, or similar agreement is effective to transfer any liability under CERCLA and the HSA, but that neither Act is intended to bar such an agreement. 42 USC §9607(e); Health & S C §25364. The Ninth Circuit has held that under §9607(e) all responsible parties are fully liable to §9607 claimants regardless of their agreements, but that private parties are free to enter into release agreements among themselves in order to assign ultimate liability. *Mardan Corp. v C.G.C. Music, Ltd.* (9th Cir 1986) 804 F2d 1454, 1459.

In *Mardan,* the court held that a release and settlement agreement between a buyer and a seller of a manufacturing property was effective to relieve the seller of liability to the buyer under CERCLA despite the lack of an express reference to CERCLA. The court also found that the release agreement was permitted under §9607(e) and was effective under state law to relieve the seller from CERCLA liability to the buyer. 804 F2d at 1458, 1460.

Courts in different circuits have construed §9607(e) differently. Some federal courts have held that parties may bargain over indemnification for, or release from, CERCLA liability under all circumstances. These courts have found the first and second sentences of §9607(e)(1) to be inconsistent, with the result that the second sentence negates the first. That section states:

> (1) No indemnification, hold harmless, or similar agreement or conveyance shall be effective to transfer from the owner or operator of any vessel or facility or from any person who may be liable for a release or threat of release under this section, to any other person the liability imposed under this section. Nothing in this subsection shall bar any agreement to insure, hold harmless, or indemnify a party to such agreement for any liability under this section.

Under this rule, the parties' agreement as to who bears liability may be effective to specify the party directly liable to third party claimants. The Ninth Circuit and other courts, however, have held that §9607(e) permits private parties to contract among themselves with respect to indemnification and contribution, but that such contractual provisions will not relieve either party from liability to the government or other §9607 claimants. A third rule was articulated by the Northern District of Ohio in *AM, Int'l, Inc. v International Forging Equip.* (ND Ohio 1990) 743 F Supp 525, which stated that §9607(e)(1) forbids giving effect to releases between tortfeasors in CERCLA suits but does give effect to indemnity agreements by parties who are not otherwise liable. See discussions in *Jones-Hamilton Co. v Kop-Coat, Inc.* (ND Cal 1990) 750 F Supp 1022, 1026, rev'd in part on other grounds sub nom *Jones-Hamilton Co. v Beazer Mat'ls & Serv.* (9th Cir 1992) 973 F2d 688; *Mardan Corp. v C.G.C. Music, Ltd., supra; Niecko v Emro Mktg. Co.* (ED Mich 1991) 769 F Supp 973.

An environmental release clause should be tailored to fit the precise circumstances of the transaction. For a typical release clause on known contamination and future discoveries of unknown contamination, see forms in §§7.62-7.63. Despite the provisions of any release, however, the California courts will probably not relieve a seller for failure to meet its disclosure obligations under Health & S C §25359.7 (see §7.36) or any other disclosures required by law.

To avoid waiving rights against third parties (see §7.21), an express provision preserving such rights should be included. For release forms containing provisions preserving these rights, see §§7.62-7.63, 7.65. On indemnification, see §7.66; for indemnification forms, see §§7.68, 7.70. See form 4.173-2 on buyer's representations and warranties, and form 4.173-6 for a release clause.

© The Regents of the University of California

§7.62 1. Form: Broad Clause Releasing Seller

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§7.48-7.80.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

7.62-1 Broad clause releasing seller

Buyer hereby releases Seller, its officers, directors, shareholders, affiliates, and subsidiaries from any and all claims, liabilities, costs, or damages that Buyer may suffer arising from (a) the existence of the soil contamination identified in Section 2 of that certain Phase I Environmental Report prepared by _ _[*name of environmental services company*]_ _ and dated _ _[*date*]_ _, a copy of which is attached to this document as Exhibit _ _, or (b) the discovery or existence after the close of escrow of any other hazardous materials on, under, or around the property, whether or not caused by Seller or any predecessor-in-interest of Seller, and whether or not known to Seller or Buyer at or before the close of escrow. Buyer expressly preserves its rights against other parties and does not release, or waive its rights to contribution against, any other party.

Comment: Clause (a) of this form must be tailored to fit the circumstances. Some attorneys include an express waiver of CC §1542 on the ground that an environmental release may constitute a general release waiving claims not known to the party executing the release. Such a waiver seems inconsistent with that section, which provides that it applies to a general release, while the environmental release clause appears to be a release of liability for specific matters and not a general release. Nonetheless, it may be better to err on the side of caution.

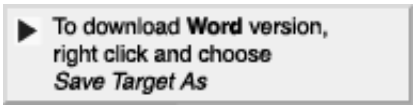
For a general release provision, see form 4.173-6.

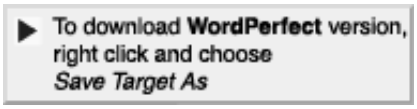
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/7 Hazardous Waste Considerations/§7.63 2. Form: Limited Clause Releasing Seller; Seller Retains Some Responsibilities

§7.63 2. Form: Limited Clause Releasing Seller; Seller Retains Some Responsibilities

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§7.48-7.80.





7.63-1 Limited clause releasing seller; seller retains some responsibilities

Buyer hereby releases Seller, its officers, directors, shareholders, affiliates, and subsidiaries from any and all claims, liabilities, costs, or damages that Buyer may suffer arising from any hazardous material identified or discovered on, in, or under the property after the close of escrow unless it (a) consists of or was caused by one or more of the chemicals, substances, or hazardous substances or wastes identified in Exhibit _ _, attached to this agreement; or (b) was caused by or permitted to occur by Seller as a result of Seller's use of the property before close of escrow. Buyer expressly preserves its rights against other parties and does not release, or waive its rights to contribution against, any other party.

Comment: The release clause can be tailored by altering the "arising from" clause in form 7.62-1 to language that reflects the parties' intent. For example, when the buyer will be responsible for remediating new contamination but the seller will continue to be responsible for any contamination that is discovered after close of escrow but is found to have been caused from chemicals used by the seller in its manufacturing process, the "arising from" clause might be modified as shown in the form above.

Clause (a) is a narrower alternative, which if usable reduces the likelihood of future litigation over who caused contamination discovered after close of escrow because it specifically identifies contaminants for which the seller is not released. The exhibit would be a schedule of chemicals or toxics used or generated by the seller in its use of the property. Before agreeing to the list, the seller would also want to make sure that the buyer does not use or generate the same substances. Clause (b) is broader but is likely to lead to litigation over which party, buyer or seller, caused the later-discovered contamination.

© The Regents of the University of California

§7.64 3. "As Is" Clauses as Release Clauses

Despite *Mardan Corp. v C.G.C. Music, Ltd.* (9th Cir 1986) 804 F2d 1454 (see §7.61), there is some risk in drafting a clause that, while not a clear release clause, purports to relieve a seller from liability for toxic contaminants that are unknown at the date of the transaction. Such provisions may be challenged under a line of cases holding "as is" clauses ineffective to release CERCLA liability. *Wiegmann & Rose Int'l Corp. v NL Indus.* (ND Cal 1990) 735 F Supp 957; *International Clinical Labs. v Stevens* (ED NY 1989) 710 F Supp 466, 469; *Mardan Corp. v C.G.C. Music, Ltd.* (D Ariz 1984) 600 F Supp 1049.

In *Wiegmann*, the court reviewed the "as is" clause, which it described as standard boilerplate language routinely included in every contract and deed transferring property owned by NL Industries (*Wiegmann & Rose Int'l Corp.,* 735 F Supp at 961), and held that it was not effective to relieve the seller of CERCLA liability. The court, comparing the case with the district court opinion in *Mardan,* stated that in *Mardan* the parties were aware that the property contained hazardous waste and that the EPA might require action to be taken, while in *Wiegmann,* the purchasers had no knowledge of the contamination. (The district court in *Mardan* addressed both an "as is" clause in the initial purchase and sale agreement between the parties and a subsequent settlement and release agreement, while the court of appeals in *Mardan* addressed only the latter.) The *Wiegmann* court concluded that (735 F Supp at 962)

> allowing an otherwise "responsible party" to avoid liability under [CERCLA] Section 107, based on an "as is" clause in the deed conveying the property, would clearly circumvent both the intent and the language of the statute. This is particularly true when the conveyance occurred prior to the enactment of CERCLA and the purchasers had no knowledge of the contamination.

Despite *Wiegmann,* the discussions in *Jones-Hamilton Co. v Kop-Coat, Inc.* (ND Cal 1990) 750 F Supp 1022, rev'd in part on other grounds sub nom *Jones-Hamilton Co. v Beazer Mat'ls & Serv.* (9th Cir 1992) 973 F2d 688, and *Niecko v Emro Mktg. Co.* (ED Mich 1991) 769 F Supp 973, and the court of appeals decision in *Mardan Corp. v C.S.C. Music, Ltd., supra,* make it clear that responsible parties are permitted to contract for a release from CERCLA liability as a buyer and a seller even if the seller has no knowledge of the contamination before the closing of the transaction as long as the contract's provisions are valid under state law. See *Mardan Corp. v C.G.C. Music, Ltd.* (9th Cir 1986) 804 F2d 1454, 1460. Apparently, the Ninth Circuit will enforce a modified disclaimer clause that clearly expresses the parties' intent to disclaim a seller's liability for toxic contamination. A seller's normal "as is" clause, with the addition of language that makes clear what the parties intended, should suffice as a disclaimer clause. See form 7.65-1. See form 4.173-2 for provisions on buyer's representations and warranties, and form 4.173-5 for an "as is" clause.

© The Regents of the University of California

§7.65 4. Form: Expanded "As Is" Clause

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§7.48-7.80.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

7.65-1 Expanded "as is" clause

Buyer agrees that, as of the close of escrow, it will be acquiring the property in "as is" condition with all faults and conditions then existing on the property, including any hazardous substances or hazardous wastes that may be located on, under, or around the property, whether known or unknown. Buyer assumes all responsibility for such faults and conditions. Buyer expressly preserves its rights against other parties and does not release, or waive its rights to contribution against, any other party.

Comment: This additional language should differentiate the clause from the "as is" clauses discussed in the district court opinions in *Mardan Corp. v C.G.C. Music, Ltd.* (D Ariz 1984) 600 F Supp 1049 and *International Clinical Labs. v Stevens* (ED NY 1989) 710 F Supp 466, both of which were held ineffective to release CERCLA liability under New York law because an as-is clause precludes only actions based on warranty theory. *Mardan Corp.,* 600 F Supp at 1055; *International Clinical Labs.,* 710 F Supp at 470. This clause also incorporates language similar to that which was found effective to release seller's liability under the Michigan Leaking Underground Storage Tank Act in *Niecko v Emro Mktg. Co.* (ED Mich 1991) 769 F Supp 973, 986. Nonetheless, until an appropriate disclaimer clause is tested in the Ninth Circuit, counsel may prefer to use an environmental release clause that at least facially conforms to the existing Ninth Circuit cases.

© The Regents of the University of California

§7.66 E. Indemnification

Although 42 USC §9607(c) applies to both release and indemnification clauses, the two types of clauses differ substantially in effect. For this reason they are discussed separately in this chapter, but many of the issues discussed in §§7.61-7.65 on the effectiveness of a release clause also apply to indemnification clauses discussed in §§7.67-7.72. The practical effect of a release clause is to relieve the released party from liability to the releasing party if suit is brought against the releasing party on matters for which the released party or parties would otherwise be liable. A release clause will not, however, bar a suit against the released party brought by a third party. An indemnity clause goes a step further and gives the indemnitee (usually the released party) a right to recover from the indemnitor (usually the releasing party) in the event of such a third party action. Some buyers may be willing to release a seller from liability for known or unknown contamination but may not be willing to take the next step and indemnify the seller for claims brought by third parties against the seller because of the contamination. As with any indemnification, the party being indemnified will want assurance that the indemnitor has adequate financial resources, and will have such resources in the future, to meet its obligations.

Attorney fees incurred in enforcing an indemnity claim are not recoverable unless the indemnity agreement expressly provides for them. See *Jacobus v Krambo Corp.* (2000) 78 CA4th 1096, 1105, 93 CR2d 425; *Otis Elevator Co. v Toda Constr.* (1994) 27 CA4th 559, 32 CR2d 404. The Ninth Circuit, however, has held to the contrary. See *DeWitt v Western Pac. R.R.* (9th Cir 1983) 719 F2d 1448.

© The Regents of the University of California

1. Seller's Indemnification of Buyer

§7.67 a. Factors to Consider

A buyer who wishes to purchase real property may want the seller to take the risk of liability for preexisting known or unknown contamination and will seek an indemnity from the seller as protection. When contamination on the property is known and the seller agrees to remediate it before close of escrow, the buyer will, at a minimum, want to be indemnified for liability arising from the seller's failure to complete a remediation or the removal process or from claims for personal injury or property damage that resulted from the contamination before the date the buyer purchased the property.

The extent of any such indemnity and the seller's willingness to provide it will depend on several factors, including:

- The severity of the environmental problem;
- The price agreed on between the parties; and
- The degree to which the parties are comfortable with the environmental investigations on which they are relying.

The enforceability of such an indemnity seems to be confirmed by the district court's holding in *Jones-Hamilton Co. v Kop-Coat, Inc.* (ND Cal 1990) 750 F Supp 1022, aff'd in part on this issue and rev'd in part on other grounds sub nom *Jones-Hamilton Co. v Beazer Mat'ls & Serv.* (9th Cir 1992) 973 F2d 688, subject to interpretation of the indemnity's effectiveness under state law. See *Mardan Corp. v C.G.C. Music, Ltd.* (D Ariz 1984) 600 F Supp 1049. Without this indemnification, a buyer would still have a claim against the seller under CERCLA and the Carpenter-Presley-Tanner Hazardous Substance Account Act (HSA) (under 42 USC §9607(a)(4)(B) and Health & S C §25363(e), respectively). However, the claim would not be as complete and may be subject to limitations. See §7.16.

Although a seller may be willing to indemnify the buyer for known contamination, many sellers will not be willing to indemnify a buyer for unknown contamination that may exist at the time of the sale but has not yet been discovered, particularly when both parties are relying on an environmental consultant's report. An alternative indemnification form that is limited to known conditions is provided in §7.68. As a practical matter, such a clause protects the buyer if the seller fails to completely remediate the known contamination, because the clause applies only when the buyer will not accept the property with the contamination, in which event the seller must remediate it. This form is also limited to an indemnity of the buyer and does not extend to the buyer's successor-in-interest.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/7 Hazardous Waste Considerations/§7.68 b. Form: Seller's Limited Indemnification of Buyer

§7.68 b. Form: Seller's Limited Indemnification of Buyer

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§7.48-7.80.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

7.68-1 Seller's limited indemnification of buyer

Seller hereby agrees to indemnify and hold harmless Buyer, its directors, officers, employees, and agents, from and against any and all costs, damages, claims, and liabilities, including reasonable attorney fees, foreseeable or unforeseeable, directly or indirectly arising from the release, treatment, use, generation, storage, or disposal on, under, or from the property of the hazardous materials identified in the environmental report before close of escrow, including, without limitation, the cost of any required or necessary remediation or removal of such hazardous materials, any cost of repair of improvements on the property or surrounding property necessitated by the remediation or removal of such hazardous materials, and the costs of any testing, sampling, or other investigations or preparation of remediation or other required plans undertaken in connection with the remediation or removal of such hazardous materials. Seller's indemnity shall survive the close of escrow. Seller expressly preserves its rights against other parties and does not release, or waive its rights to contribution against, any other party.

Comment: To avoid making the effect of this clause broader than intended, counsel must carefully define both the hazardous materials identified in the environmental report and the areas of the property affected.

© The Regents of the University of California

2. Buyer's Indemnification of Seller

§7.69 a. Assumed Toxic Condition

A seller who is relying on the buyer to complete remediation, or who has reduced the price of the property as a trade-off for the buyer to accept it with the contamination, will want indemnification by the buyer for all claims arising from the condition of the property at the time of the sale or from the buyer's failure to proceed with or properly perform the remediation or removal. Such an indemnification would give the seller the right to recover from the buyer for:

- Third party claims for personal injury or property damage arising after the close of escrow because of conditions existing before close of escrow;
- Third party claims for property damage or personal injury arising from the buyer's actions in the course of remediating or removing the assumed contamination; and
- Costs resulting from remediation orders or claims for response costs or other sums brought by the government or third parties.

For a form by which the buyer indemnifies the seller for all contamination that existed before or is discovered after close of escrow, see form 7.70-1.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/7 Hazardous Waste Considerations/§7.70 b. Form: Buyer's Broad Form Indemnification of Seller

§7.70 b. Form: Buyer's Broad Form Indemnification of Seller

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§7.48-7.80.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

7.70-1 Buyer's broad form indemnification of seller

Buyer hereby agrees to indemnify and hold harmless Seller, its directors, officers, employees, and agents from and against any and all costs, damages, claims, and liabilities, including reasonable attorney fees, foreseeable or unforeseeable, directly or indirectly arising from any release, treatment, use, generation, storage, or disposal of hazardous materials on, under, or from the property at any time before or after close of escrow, including, without limitation, the cost of any required or necessary remediation or removal of such hazardous materials, any costs of repair of improvements on the property or surrounding properties necessitated by such remediation or removal and costs of any testing, sampling, or other investigation or preparation of remediation or other required plans undertaken prior to such remediation or removal. Buyer expressly preserves its rights against other parties and does not release, or waive its rights to contribution against, any other party.

Comment: The "arising from" clause can be modified to address only known contamination, *e.g.,* "arising from those certain hazardous materials identified in an environmental report prepared by John Doe Environmental Services of January 1, 2007, a copy of which is attached as Exhibit A."

© The Regents of the University of California

c. Postclosing Discoveries

§7.71 (1) Preexisting Conditions

When negotiating the buyer's indemnification of the seller for claims related to toxic contamination, the parties must consider whether the indemnification will cover only preexisting conditions that the parties were aware of at the time they entered into the purchase and sale agreement (or at the time of any applicable amendment to the agreement), or whether the indemnification will extend to matters that may exist at the closing but are undiscovered. See form 7.70-1 and Comment. This issue is somewhat similar to the issue of what should be covered in a release clause (see §§7.61-7.65), and counsel must rely on the bargaining power of each party and on the agreement that is ultimately reached. Usually, a buyer who accepts contaminated property, and assumes responsibility for its remediation, has evaluated the risk that the property may contain more contamination. Counsel's role is then to learn the extent of the risk the buyer is prepared to assume and draft the agreement accordingly. Cross-indemnities may be necessary, in which the buyer indemnifies the seller for known contamination and the seller indemnifies the buyer for additional problems discovered during remediation. One risk of cross-indemnification, however, is that a buyer's broad indemnity, if it becomes public knowledge, may then become an invitation to claimants to initiate lawsuits.

© The Regents of the University of California

§7.72 (2) Conditions Caused by Buyer After Closing

A seller may wish to include an indemnification provision regarding the buyer's future use of the property when the buyer will continue an industrial use. The indemnity should address all contamination attributable to the buyer's activities on the site after closing. If the indemnity clause later becomes the subject of litigation, the primary issues will be (1) proving the cause of the contamination, and (2) establishing which party has the burden of proof. Burden of proof can be addressed in the agreement, but it may be difficult to draft a provision that addresses as yet unknown evidence. Typically, the environmental reports prepared by the parties before closing will provide evidence of the conditions at closing, and any new conditions would then, prima facie, be conditions caused by the buyer.

© The Regents of the University of California

§7.73 F. Remediation

If the property is found to be affected by toxic contamination but the parties still wish to proceed with the transaction, they must agree on who will pay for the remediation or removal and who will be primarily responsible for its completion. Reaching such agreements might at first seem to be fairly simple, but many transactions fail because the parties cannot agree on these issues. The party acquiring the property wants the property to be as free of contamination as possible while bearing as little of the remediation or removal cost as possible, and the selling party wants to remove or remediate only as much contamination as is absolutely necessary and at the lowest cost possible. Given these two viewpoints, it may be surprising that parties are ever able to agree on remediation provisions.

The more that is known about the extent and nature of the contamination and the cost and nature of the remediation effort required, the easier it will be to negotiate these provisions. It is not unusual in complex situations for the parties, after discovering previously unknown contamination, to amend the purchase and sale agreement to address the scope of, and responsibility and time frames for, further investigations, and to add a second amendment later to cover remediation after the investigations are completed. See also §§7.10-7.31 on remediation.

© The Regents of the University of California

§7.74 1. Responsibility for Costs

There is no standard that governs liability for the costs of remediation. They can be allocated completely to either party or can be shared in any number of ways. Most transactions fall into one of two categories:

- The seller will bear all responsibility for the performance and costs of remediation (to be done either before or after closing), and the purchase price is based on the fair market value of the property in uncontaminated condition; or
- The buyer will assume the complete cost of and responsibility for remediation, with an adjustment to the purchase price based on remediation cost estimates from environmental consultants.

If the transaction does not fit either category and the parties decide to share the remediation costs, many allocation methods are possible. The parties may agree to split the costs based on a percentage ratio or on the various tasks undertaken by each party. They may agree that the seller will be responsible for cleaning up only certain items, while the buyer takes a partial reduction in the purchase price and will be responsible for other items.

PRACTICE TIP: The benefit of sharing the costs on some prorata basis is that both parties will then be conscious of the cleanup costs and will have an incentive to focus on the level of contamination to be remediated or removed. If the cost is borne solely by one party, the other party has less incentive to cooperate with governmental agencies to establish alternative limits for the level to which the contamination must be remediated. However, remediation cost estimates are uncertain, and buyers (other than those willing to assume all cost responsibility) should be wary of entering a prorata sharing arrangement without obtaining either a cap on their share of costs or very precise cost estimates.

© The Regents of the University of California

§7.75 2. Control of Process

Regardless of who will pay for the remediation, both parties will want some degree of control over establishing and implementing the remediation or removal program. Usually, before any work is begun, a remedial action plan must be prepared and approved by the governmental agencies that will have control over the remediation process. Typically, the lead agency will be the Department of Health Services or County Health Care Agency, for soil contamination, or the Regional Water Quality Control Board, for groundwater contamination. A seller may be willing to forgo any control if the buyer agrees to assume all obligations for the remediation and its costs, close escrow before remediation is completed, and release and indemnify the seller from and for claims arising from the particular contamination. The seller still assumes some risks in such circumstances, but a client may choose to risk future claims in order to be relieved of current cash expenditures.

PRACTICE TIP: When the remedial action plan can be prepared, agreed on by the parties, and approved by the governmental agencies before close of escrow, the parties may not be as concerned about the degree of control each has over the actual performance of the work. However, if the work includes preparing a remedial action plan and obtaining the governmental agencies' approval of it, both parties must make sure that they are adequately involved in the process and that they will be comfortable working with each other throughout the process.

Once the remedial action plan has been approved, the parties will need to address how, or whether, they will share the decision of selecting or replacing both an environmental consultant and the contractors who will perform the work. They must also decide how to perform the work so as to cause the least interference with the use and operation of the property. They may also wish to address whether newer, more efficient technology could be used in remediation if it becomes available during the process.

Typically, the environmental consultants that each party uses in the process will have been selected by the parties before or during the escrow period, but if the party primarily responsible for remediation later wishes to change consultants, the other party may want to be involved in the decision. This issue often arises when the individual consultant who is primarily responsible for the project changes companies. Similarly, the party who is not primarily responsible may also want to be involved in the selection of a general contractor for the remediation work. If each party has its own consultant, the parties will also need to decide whether both consultants will meet with the relevant governmental agencies throughout the process or whether only the consultant for the party primarily responsible for completing the remediation will attend such meetings. On one hand, both parties will want to feel that they are fully informed on the status of the process. On the other hand, if fewer people attend, the meetings can retain a more informal nature and sometimes run more efficiently and effectively.

© The Regents of the University of California

§7.76 3. Disposal

Under both the Resource Conservation and Recovery Act of 1976 (RCRA), as amended (42 USC §§6901-6992k) and the Hazardous Waste Control Law (HCL) (Health & S C §§25100-25257.1), any hazardous waste that is transported or disposed of must be properly documented. 42 USC §§6922(a)(5), 6924(a)(1)-(2), (7); Health & S C §25160. The party responsible for disposing of toxic contamination as part of a remediation or removal process will be listed on state waste manifests as the generator of the waste, and thus will be considered a liable party if the landfill where the waste is disposed of later requires remediation. 42 USC §§6922(a)(5), 6924(a)(1)-(2), (7); Health & S C §25160. To the extent that liability exists for the future costs of cleaning up a site, the party who is responsible for the disposal and who thereby becomes the record owner of the contaminated waste will be a likely defendant for some of the costs of a subsequent cleanup of the site. 42 USC §9607(a)(3); see *Chemical Waste Mgmt., Inc. v Armstrong World Indus.* (ED Pa 1987) 669 F Supp 1285. Thus, whether the final remediation of the property occurs before or after close of escrow, most buyers require that any contamination be disposed of under a disposal permit issued in the seller's name.

© The Regents of the University of California

§7.77 4. Agency Assurances—Comfort Letter and Prospective Purchaser Agreement

One uncertainty facing buyers and sellers of contaminated property is the type and extent of remediation work that will be required by the lead agency. Reflecting the national "brownfields" trend (the recent tendency of regulatory agencies to be more realistic in setting remediation requirements and thereby encouraging development or redevelopment of contaminated properties), the California Department of Toxic Substances Control (DTSC) has adopted a policy, largely followed by the California State Water Resources Control Board, to provide owners and prospective purchasers with assurances about who will be held liable for existing contamination and the type and extent of remediation work that will be required. See California Department of Toxic Substances Control, *Prospective Purchaser Policy*, Policy No. EO-96-005-PP (July 3, 1996); California State Water Resources Control Board, *Guidance Memo Regarding Brownfields: Prospective Purchaser Agreements and Agreements With Current Owners for Cleanup of Polluted Property* (July 9, 1996). The U.S. Environmental Protection Agency (EPA) has adopted a similar policy. See EPA, *Guidance on Agreements With Prospective Purchasers of Contaminated Property and Model Prospective Purchaser Agreement,* 60 Fed Reg 34789-34792 (1995).

Under the State Water Resources Control Board's version of the programs, these assurances can take the form of either a "comfort letter" or a "prospective purchaser agreement." At the most basic level, a Regional Water Quality Control Board (RWQCB) can issue a "comfort letter," which does not constitute a formal legal release but advises the recipient about the investigation and remediation work performed to date and identifies which party or parties the RWQCB is holding responsible for contamination and remediation. Particularly in situations in which the contamination has been characterized and a remedial action plan has been approved and substantially implemented, a comfort letter may provide sufficient assurance to allow the parties to complete the transaction.

When more detailed and binding assurances are needed, a prospective buyer can negotiate with the RWQCB or the DTSC and enter into a "prospective purchaser agreement." The terms of the agreement typically include a detailed scope of remediation work and a covenant by the buyer to undertake the work, as well as a covenant by the RWQCB or the DTSC not to sue the buyer if the agreed-on remediation work is completed. The prospective purchaser agreement facilitates the sale of the property by allowing the buyer to identify an upper limit on the type and cost of remediation work that will be required, which allows the buyer to understand and more accurately quantify the expense and timing risks associated with the contamination and to establish a more reliable budget for the acquisition and use of the property.

© The Regents of the University of California

G. Securing Remediation Costs

§7.78 1. Remediation Cost Estimate

If property is known to be contaminated before the sale is closed but will not be remediated until after closing, the party responsible for remediation should be asked to provide proof of financial ability to complete remediation or removal, or provide adequate security to ensure that funds will be available to complete the cleanup. There are several mechanisms that may be used to ensure that funds will be available to cover remediation costs. See §§7.79-7.83.

© The Regents of the University of California

§7.79 2. Escrow of Funds

If the seller is responsible for the costs of remediation after closing, a new escrow may be funded from the purchase price otherwise payable to the seller at the time of closing. If the buyer is responsible for the remediation, a new escrow can also be established, but the buyer will need to fund the new escrow separately. The provisions requiring the creation and governing of the new escrow can be included (1) as part of the purchase and sale agreement, (2) as an amendment to it, or (3) in a separate escrow agreement to be executed by the parties before or concurrently with the close of escrow. Generally, it is preferable to have a separate escrow agreement (because the escrow agent is typically a party to the escrow agreement, but not to the purchase and sale agreement), and to provide in the purchase and sale agreement only for disbursement to the new escrow.

The separate escrow agreement will include the following:

- Instructions to the escrow holder for the investment of the funds that are deposited into or remaining in escrow from time to time;
- Instructions for disbursement of funds during the term of the escrow to pay for the costs of the remediation, subject to appropriate approvals of disbursements by one or both parties; and
- Provisions for additional deposits into escrow when necessary and if applicable to the transaction.

The escrow agreement should also state that the amount deposited into the escrow account does not constitute a limitation on the responsible party's obligation to make expenditures to complete the remediation of the property, unless the parties have reached an agreement that the liability of the party funding the escrow for the costs of remediation will be capped at the escrowed amount. A form remediation escrow agreement is set forth in §7.80.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/7 Hazardous Waste Considerations/§7.80 3. Form: Remediation Escrow Agreement

§7.80 3. Form: Remediation Escrow Agreement

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§7.48-7.80.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

7.80-1 Escrow agreement

ESCROW AGREEMENT

This ESCROW AGREEMENT (Agreement) is made and entered into as of _ _[*date*]_ _, by and between _ _[*name*]_ _ (Seller) and _ _[*name*]_ _ (Buyer).

A. Prior to the date of this Agreement, Buyer and Seller entered into a purchase and sale agreement (Purchase Agreement), dated _ _[*date*]_ _, providing for the sale by Seller to Buyer and the purchase by Buyer from Seller of certain real property and the improvements located on it (Property) as more particularly described in the Purchase and Sale Agreement.

B. Buyer and Seller now desire to open and to provide the terms of and instructions for an escrow (Escrow), to be opened with _ _[*name of escrow company*]_ _ (Escrow Holder), for the costs of _ _[*e.g., remediating groundwater contamination*]_ _ under a portion of the Property as identified in that certain Environmental Report dated _ _[*date*]_ _, prepared by _ _[*name of environmental consultant*]_ _ regarding the Property (Contamination) in accordance with an Approved Remediation Plan (as defined in this Agreement).

NOW, THEREFORE, in consideration of the recitals set forth above and for other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, the parties agree as follows:

1. *Opening of Escrow.* On the Closing under the Purchase Agreement (as that term is defined in the Purchase Agreement), the Escrow shall be established with Escrow Holder by Seller's deposit into the Escrow of the sum of _ _[*amount*]_ _ Dollars (_ _[*dollar amount*]_ _) from the proceeds otherwise due Seller from the Closing under the Purchase Agreement.

2. *Investment of Funds.* All funds deposited with Escrow Holder for the Escrow, or which may from time to time be held by Escrow Holder in the Escrow, shall be placed in such investments as the parties to this Agreement may from time to time direct. If Escrow Holder has not received instructions on the investment of funds before the initial deposit of funds is made into Escrow or the maturity of any investment into which the funds in Escrow are deposited, then Escrow Holder shall, until Escrow Holder receives further instructions, deposit the funds then held by it in the Escrow into an interest-bearing account with a financial institution reasonably selected by Escrow Holder. Escrow Holder shall have no responsibility for any investment decisions made by the parties to this Agreement.

3. *Instructions.* This Agreement shall constitute Escrow Holder's instructions regarding Escrow. The parties agree to execute any further reasonable instructions that Escrow Holder may request that are not inconsistent with this Agreement.

4. *Disbursements to Seller.* Seller may instruct Escrow Holder to disburse funds from the Escrow from time to time to pay costs (Costs) incurred for or in relation to the remediation, including without limitation, costs of preparing and obtaining government approvals of remediation plans for the Contamination (such plans, after approval of the same by those governmental agencies having jurisdiction over the Property and subject to such modifications as may from time to time be required by such agencies, are referred to collectively as the "Approved Remediation Plan"); costs of performing work required under the Approved Remediation Plan; costs of design, construction, or installation of any facilities required under the Approved Remediation Plan; and prepayments or deposits required to order materials.

Escrow Holder shall disburse funds to such parties as Seller may identify at least _ _[*e.g., 15*]_ _ days and no more than _ _[*e.g., 30*]_ _ days after Escrow Holder's receipt from Seller of a demand for payments accompanied by all of the following:

(a) A schedule and copies of the invoices that Seller is instructing Escrow Holder to pay;

(b) The amount of costs that Seller is instructing Escrow Holder to pay on account of each such invoice and the party to whom such amount should be paid;

(c) An address to which payment on account of each such invoice should be sent.

5. *Disbursement Disputes.* If, within _ _[*e.g., 15*]_ _ days after Escrow Holder receives an instruction to disburse funds in payment of an invoice in accordance with section _ _[*e.g., 5*]_ _ of this Agreement, Buyer determines that the payment which Escrow Holder has been instructed by Seller to make is for an improper purpose or is for work not yet performed (other than prepayments or deposits for materials) in relation to the remediation of the Contamination, then Buyer may, within the _ _[*e.g., 15*]_ _-day period, provide notice to Escrow Holder and Seller that Buyer disapproves Seller's disbursement instruction. Such notice shall identify the particular invoice on which payment is disapproved, the amount of the payment that is disapproved, and the reason for the disapproval. On receipt of such notice, Escrow Holder shall continue to make all disbursements that it has been instructed to make other than the disapproved item. Escrow Holder shall retain in Escrow the funds that would have been disbursed with regard to the disapproved amount until Escrow Holder receives further instructions from Buyer and Seller or the dispute as to such disapproved item is otherwise resolved.

6. *Resolution of Disputes.* If Buyer disapproves any disbursement that Escrow Holder was instructed to make by Seller, the parties shall, within _ _[*e.g., 30*]_ _ days after Buyer's notice of such disapproval, seek to reach an agreement on whether the disputed amount should properly be included within Costs and whether the work on account of which such invoice was submitted to Seller by a third party was performed. If the parties cannot agree on a resolution of the dispute within the _ _[*e.g., 30*]_ _-day period, then each party shall, within _ _[*e.g., 10*]_ _ days after the end of such _ _[*e.g., 30*]_ _-day period, select a qualified environmental consultant, and the two qualified environmental consultants so selected shall, within _ _[*e.g., 15*]_ _ days after both are selected, each determine whether all or part of the disputed amount should be disbursed from Escrow. The average of the amounts that each environmental consultant determines shall constitute the amount that Escrow Holder shall be instructed to disburse. Buyer shall pay the fees and costs of the environmental consultant selected by Buyer, and Seller shall pay the fees and costs of the environmental consultant selected by Seller.

7. *Final Disbursement*

(a) On completion of the remediation, Seller's environmental consultant shall issue a letter (Release Letter), certifying that the remediation is complete. On delivery of a copy of such letter to Escrow Holder and to Buyer, Escrow Holder is hereby instructed to disburse to Seller all funds remaining in the Escrow.

(b) If Escrow Holder has not received such letter by, on, or _ _[*e.g., 2 years*]_ _ after the date of this Agreement, then Escrow Holder shall disburse to Seller all funds remaining in Escrow, whether or not the funds are the subject of a dispute between Seller and Buyer with regard to a previous payment instruction, unless before such date Escrow Holder receives a joint instruction from Buyer and Seller to continue the Escrow. If Escrow Holder receives such joint instruction, the Escrow shall be extended for a period of _ _[*e.g., 1 year*]_ _, at which date the provisions of this section 7(b) related to extending the Escrow shall again be applied. Seller and Buyer agree to execute a joint instruction to Escrow Holder to continue the Escrow if, before the applicable date for disbursement of funds under this section 7(b), remediation is not complete or the Seller's environmental consultant has not issued the Release Letter.

8. *Escrow Holder's Fees and Expenses.* Escrow Holder's fees and expenses shall be paid half by Seller and half by Buyer.

9. *Conflicting Demands*

(a) If any disagreement arises between Seller and Buyer that results in conflicting or adverse claims or demands being made in connection with this Agreement or the Escrow, Escrow Holder shall be entitled, at its

option, to refuse to comply with any such claim or demand, as long as the disagreement shall continue, and, in so doing, Escrow Holder shall not become liable for damages or interest to any party for its failure or refusal to comply with the conflicting or adverse claims or demands. Escrow Holder shall be entitled to continue to so refrain and refuse to act until the conflicting or adverse claims or demands have been resolved in accordance with the procedures set forth in this Agreement or by a court of competent jurisdiction;

(b) Escrow Holder may also file a suit in interpleader to have the respective rights of any adverse claimants adjudicated, and deposit with the court all documents and funds held by Escrow Holder under this Agreement. In this event, Seller and Buyer shall each pay half of Escrow Holder's costs, and attorney fees incurred in the action shall be paid by the losing party, or in such other manner as the court may order.

10. *Duties of Escrow Holder.* Seller and Buyer agree that Escrow Holder's duties are only those specified here, that such duties are purely ministerial in nature, and that Escrow Holder shall not incur any liability except for willful misconduct or gross negligence as long as it has acted in good faith.

11. *Resignation or Removal of Escrow Holder.* Escrow Holder shall have the right, on _ _[*e.g., 30*]_ _ days' prior written notice to Seller and Buyer, to resign from its position as Escrow Holder, as long as it finds a replacement Escrow Holder that is acceptable to both Seller and Buyer, before the effective date of Escrow Holder's resignation. Seller and Buyer shall have the right, on _ _[*e.g., 20*]_ _ days' prior written notice to Escrow Holder, to remove and replace Escrow Holder with an escrow holder mutually acceptable to Seller and Buyer. In the event of any such resignation or removal, Escrow Holder shall be entitled to receive its reasonable costs and expenses incurred as of the effective date of its resignation or removal.

12. *General Provisions*

(a) Notices. Any notice given in connection with this Agreement shall be given in writing to the parties at their respective addresses set forth below. Any notice, instruction, or demand given to Escrow Holder by either party shall be provided to the other party by the same notice method and concurrently with the giving of such notice to Escrow Holder. Any such notice shall be given by personal delivery or United States mail, postage prepaid, and shall be deemed to have been delivered, if by personal delivery, on the delivery of the notice, or if by United States mail, _ _[*e.g., 3*]_ _ days after the deposit of the same into the United States mail, postage prepaid.

[*List parties' addresses*]

Any party to this Agreement may change the address for notice specified above by providing notice of such change of address in accordance with the provisions of this section.

(b) Further Assurances. Seller and Buyer agree to execute and deliver such other instruments and documents and take such other actions as may be reasonably required in order to effectively complete the objectives contemplated by this Escrow Agreement.

(c) Captions and Headings. The captions and section headings used in this Escrow Agreement are inserted for convenience of reference only and are not intended to define, limit, or affect the interpretation or construction of any term or provision of this Agreement.

(d) Attorney Fees. In the event of any dispute arising out of the terms of this Agreement, the prevailing party or parties in the dispute shall be entitled to recover costs of suit, including attorney fees.

(e) Governing Law. This Agreement shall be governed by and construed in accordance with the laws of the State of California.

IN WITNESS WHEREOF, this Escrow Agreement is made and executed as of the date first set forth above.

Date: _ _ _ _ _ _ **Seller:**

_ _[*Name of entity*]**_ _,**
a _ _[*specify entity, e.g., California corporation*]**_ _**

By: __[*Signature*]**__**

Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

Date: _ _ _ _ _ _ **Buyer:**

_ _[*Name of entity*]_ _,
a _ _[*specify entity, e.g., California corporation*]_ _

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

We agree to act as Escrow Holder in accordance with the terms of this Escrow Agreement.

Date: _ _ _ _ _ _ _ _[*Name of Escrow Company*]_ _

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

Comment: See discussion in §7.79 on escrow of funds.

© The Regents of the University of California

§7.81 4. Letters of Credit

The responsible party's obligation to advance remediation funds may be secured by a letter of credit in favor of the party for whose benefit the remediation obligation is being secured. The amount of the letter of credit may be the estimated cost of remediation or an amount that would, in effect, constitute liquidated damages to the benefited party if the responsible party should fail to perform its obligations. The benefited party, however, incurs the risk that remediation costs might eventually exceed the amount of the letter of credit. Because most letters of credit have a limited term, the parties will need to agree that the letter of credit will be renewed before it expires unless remediation has then been completed, and that the letter of credit may not be drawn on if it is not so renewed in a timely manner.

© The Regents of the University of California

§7.82 5. Guaranty

If the entity that owns the property and is agreeing to be financially responsible for the remediation is a shell subsidiary or is thinly capitalized, the party for whose benefit the work will be performed will probably wish to obtain a guaranty from the performing party's parent company or affiliated entities or such entity's individual shareholders, as the case may be. Such a guaranty will constitute a suretyship obligation and, much like a loan guaranty, will be subject to suretyship laws (CC §§2787-2856) and existing case law on guaranties, although the guarantor can waive most rights. See generally California Real Estate Finance Practice: Strategies and Forms, chap 6 (Cal CEB 2000).

© The Regents of the University of California

§7.83 6. Offset Against Buyer's Note

One creative solution for securing remediation costs can be used when the seller is accepting a promissory note for part of the purchase price. The buyer can require an offset, against the balance due on the note, of remediation costs incurred but not paid by the seller. The seller should be careful about which expenses the buyer is permitted to offset. For example, a provision allowing the buyer to take an offset against the note if the seller fails to complete remediation will almost certainly end in litigation. Offsets are best when they are permitted only for known established amounts or amounts that can be quickly established by an impartial third party. If the seller refuses to complete the remediation after receiving written notice from the buyer that work has stopped, an offset provision might permit the buyer to offset the amount that a consultant estimates as the remaining cost of the remediation work. Alternatively, the offset might be only for out-of-pocket costs actually incurred and paid and evidenced by invoices. Once again, the offset should not be a bar to further liability if actual costs later incurred by the buyer exceed the amount offset. Such an offset will impair the negotiability of a promissory note, and the seller should reject it if it is important to have the flexibility to sell the note before it matures.

© The Regents of the University of California

H. Miscellaneous Provisions

§7.84 1. Arbitration Clause

The parties may wish to provide for the arbitration of disputes between them over the performance or the costs of the remediation. If the disputes to be arbitrated arise under the purchase and sale agreement, the form and content of the arbitration clause in the agreement must comply with CCP §§1298-1298.8. These sections contain the requirements for type size and style, for a notice on the effect of the provision, and for separate initialing by the parties. See §4.150. See sections 9.5.1-9.5.2 in form 4.177-5 for provisions on alternative dispute resolution.

© The Regents of the University of California

§7.85 2. Access to Property

If a seller will be obligated to perform the remediation work after closing, whether at its own expense or partially at the buyer's expense, or if it wants the right to monitor the progress of remediation being performed by the buyer after closing, the seller will need a postclosing right of access to the property as needed to complete the remediation or perform the monitoring. Such access rights can be in the form of a right-of-entry provision in the purchase and sale agreement, in a separate agreement that includes the seller's obligations on the remediation, or in a separate license or easement agreement. The parties' selection of the appropriate documentation should consider the possibility that the buyer will sell the property to a third party before remediation is completed, the types of facilities that may need to be installed on the property to complete the remediation, and the nature of the work that must be performed even if no facilities will be installed. If an easement is the access right selected, it should be recorded and should be drafted as an easement in gross.

See §8.68 on options for an illustrative form of access provisions.

© The Regents of the University of California

III. INSURANCE MATTERS

§7.86 A. Title Insurance Products

Environmental contamination has seldom been covered by recorded instruments or disclosed by surveys, so title insurance companies are not very useful sources for protection from a claim for toxic contamination. The California Land Title Association (CLTA) policies do not normally cover off-record matters, and the 2006 American Land Title Association (ALTA) form specifically excludes from coverage "[a]ny law, ordinance, permit or governmental regulation… relating to… environmental protection, or the effect of any violation of these laws, ordinances or governmental regulations…."

Title insurance companies will issue CLTA Endorsement No. 110.9 to a lender's policy, assuring that there are no environmental liens of record or filed in the United States District Court for the district in which the land is located. On environmental liens and title insurance, see California Title Insurance Practice §§4.6, 6.62, 6.86, 7.17, 11.63-11.64 (2d ed Cal CEB 1997). On endorsements protecting against environmental liens, see Title Ins §§8.77-8.78. On the effect of contamination on the marketability of property under a title insurance policy, see Title Ins §§6.25, 11.62.

It may be beneficial to obtain a chain of title search by a reputable title company to identify the historic owners and lessees of a parcel of property. The search may not be helpful if the names of the companies appearing in the chain of title are unrecognizable; however, it would be useful to know, for example, that for 20 of the last 30 years the property was owned by ABC Chemical Manufacturing. A chain of title review is an important component of establishing that "all appropriate inquiries" have been made into previous ownerships and uses, as required for the innocent landowner defense. See §7.24. Although the "all appropriate inquiry" rule does not on its face require a chain of title report, it does require the review of "historical documents," which "may include" chain of title documents. 40 CFR §312.24(a). Thus, failure to search the chain of title may allow a future plaintiff to argue that the defendant's inquiry was insufficient. Furthermore, to the extent chain of title searches become customary for Phase I Reports in the future, or are now customary in particular areas or circumstances, they may become prerequisites to an innocent landowner defense.

If a prior use of the property disclosed by the Phase I Report creates concern about potential contamination, a chain of title search might be useful in identifying the parties that owned the property during the time period in which contamination is thought to have occurred in order to permit contact with that owner or owners. A chain of title search would also benefit a property owner that finds itself the owner of contaminated property and is attempting to identify the parties that might have caused the contamination in order to seek a recovery or information from such parties, or to identify potential defendants. On chain of title guaranty, see Title Ins §9.18.

For a sample provision on buyer's closing conditions regarding title, see section 6.1.1 in form 4.174-1.

© The Regents of the University of California

§7.87 B. Environmental Liability Insurance

The insurance industry offers coverage to manage the risk of unknown contamination. For example, property transfer liability insurance, which can be very useful in the sale of real property, provides coverage against the following risks:

- Cleanup costs for contamination existing on the property on the closing date but not discovered until a later date within the policy period;
- Cleanup costs for contamination known to exist on the property on the closing date, not then required to be cleaned up, but required by a governmental agency to be cleaned up at a later date during the policy period;
- Bodily injury, property damage, and other third party claims arising from contamination on the property or migrating off the property; and
- Costs of defense.

The insurer or its broker ordinarily will conduct a due diligence review of the property to assess the underwriting risk, and coverage is usually written on a claims-made-and-reported basis. Premium costs, although substantial, have fallen in recent years as the market for such products has become more competitive. Such coverage provides a way to allocate responsibility away from both the seller and the buyer and to establish with greater certainty their respective liabilities for contamination discovered after the closing.

© The Regents of the University of California

IV. LENDER CONCERNS

§7.88 A. Nature of Lender's Liability and Underwriting

Before financing a real property purchase, a lender will evaluate how contamination—existing or potential—could affect the lender's risk in making the loan or realizing on the security. To complete a purchase and sale transaction, most buyers and sellers will need to address the lender's concerns.

The secured-creditor exemption in CERCLA, as amended, gives lenders some protection by excepting from the definition of an "owner or operator" persons who hold "indicia of ownership" primarily to protect their security interest "without participating in the management" of the property. 42 USC §9601(20)(A). Thus, a city was still eligible for the secured-creditor exemption, even though its initial motivation for purchasing land was to further economic development, as long as the city "'[held] indicia of ownership primarily to protect' its security interest in the property during the period when the pollution occur[red]." *Monarch Tile, Inc. v City of Florence* (11th Cir 2000) 212 F3d 1219, 1223.

The courts have had difficulty applying the "participating in the management" element of the exemption, as the following brief review of the case law shows:

- *Management criteria.* Although early cases distinguished between financial and operational management, the Eleventh Circuit Court of Appeals ruled that a lender may lose the secured-creditor exception by becoming involved in day-to-day operational management or by participating in the financial management "to a degree indicating a capacity to influence the corporation's treatment of hazardous wastes." See *U.S. v Fleet Factors Corp.* (11th Cir 1990) 901 F2d 1550, 1557. The breadth of the language in *Fleet Factors* caused some concern that loan provisions allowing a lender to participate in operational management, even if unenforced, would be sufficient to trigger liability. These concerns were assuaged when the Ninth Circuit Court of Appeal held in *In re Bergsoe Metal Corp.* (9th Cir 1990) 910 F2d 668, 672, that "there must be *some* actual management of the facility before a secured creditor will fall outside the exception." (Emphasis in original.)
- *Acquisition of property.* Whether or not a lender was protected under the secured-creditor exemption while it was a lender, if it later acquires the property (*e.g.,* at a foreclosure sale), the lender becomes liable as an owner. *Guidice v BFG Electroplating & Mfg. Co.* (WD Pa 1989) 732 F Supp 556, 563; *U.S. v Maryland Bank & Trust Co.* (D Md 1986) 632 F Supp 573, 579. But see *U.S. v Mirabile* (ED Pa 1985) 1985 US Dist Lexis 15411, 15 Envtl L Rep 20992 (4 months' time as owner insufficient to create liability as "owner" under CERCLA).
- *Short-lived EPA guidelines.* The EPA attempted to provide some guidelines for lenders on what constituted actual management, but the court in *Kelley v EPA* (DC Cir 1994) 15 F3d 1100 vacated those regulations on the ground that the EPA lacked statutory authority to "define liability for a class of potential defendants" by regulation. 15 F3d at 1107. The EPA then removed the regulations in complying with a presidential directive to remove obsolete or unduly burdensome regulations.
- *1996 Asset Conservation Act.* The Asset Conservation, Lender Liability, and Deposit Insurance Protection Act of 1996 (Subtitle E of the Omnibus Appropriations Act (Pub L 104-208, 110 Stat 3009)) gave lenders further protection from liability under CERCLA. A foreclosing lender is exempt from the definition of "owner or operator" if the lender did not participate in management of the property before foreclosing and, after foreclosing, seeks to sell, release (in the case of a lease finance transaction), or otherwise divest the property at the earliest practicable, commercially reasonable time on commercially reasonable terms, taking into account market conditions and legal and regulatory requirements. 42 USC §9601(20)(E). Title 42 USC §9601(20)(F) provides the following:
- To "participate in management" requires more than merely having the capacity to influence, or the unexercised right to control; and
- A lender holding indicia of ownership primarily to protect a security interest "shall be considered to participate in management only if, while the borrower is still in possession of the [property] encumbered by the security interest," the lender exercises day-to-day decision-making control over environmental compliance of the

property.

For further discussion of this legislation, see California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 12 (4th ed Cal CEB 2009).

In 1996, the California legislature enacted Health & S C §§25548-25548.7 to dispel or minimize uncertainties about "the type of lender and fiduciary conduct that will not incur liability for hazardous material contamination." Health & S C §25548(b). For detailed discussion of the state legislation, see Mortgage Deed of Trust Foreclosure, chap 12.

Because of the potential for liability, institutional lenders now routinely include as part of the underwriting process an assessment of the actual or possible effects of toxic contamination on the property; such an assessment should also be part of the private lender's due diligence analysis. Although the 1996 state and federal statutes that attempted to minimize lenders' concerns may provide some comfort regarding the scope of liability, many lenders continue to seek additional comfort either from underwriting analysis (showing that a resale of the property after foreclosure would enable the lender to recover both its loan amount and its share of any cleanup costs) or from the borrower in the form of an indemnification or other provisions.

© The Regents of the University of California

§7.89 B. Loan Application Provisions

Under most loan applications, the lender must be given a Phase I Environmental Report from an environmental consultant approved by the lender, along with the balance of the due diligence materials, before the lender will issue the loan or a firm commitment for it. If the lender requires a commitment fee before it completes any environmental reviews, the buyer-borrower will want to learn whether all or part of that fee is recoverable if the lender disapproves of the environmental reviews.

Some loan applications require that, in addition to providing the lender with a Phase I Environmental Report, the borrower must represent and warrant to the lender that it knows of no toxic contamination affecting the property at the time of applying for the loan.

© The Regents of the University of California

§7.90 C. Loan Document Provisions

Lenders often include provisions on environmental contamination in their loan documents, and buyers negotiating the purchase of property should be aware of the lender's requirements. Sellers, too, should be prepared to address lenders' concerns in order to facilitate a purchase and sale transaction. The lender's rights were substantially enhanced in 1992 by significant exceptions to the one-action rule of CCP §726 and other California antideficiency laws (CCP §§564(c)-(e), 726.5, 736; CC §2929.5). See §§7.90-7.95.

One result of these amendments is that fewer lenders use separate environmental indemnity agreements. Separate indemnities were previously used to minimize the risk of antideficiency protections, which barred recovery after foreclosure under environmental indemnity provisions in deeds of trust. See §7.95. Because these statutes confirm that environmental indemnities are enforceable whether or not such provisions are in the deed of trust, most lenders now include such provisions in their deeds of trust. See California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 4 (4th ed Cal CEB 2009).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/7 Hazardous Waste Considerations/§7.91 1. Representations

§7.91 1. Representations

In addition to requiring environmental reviews of the property before making a loan, a lender will expect the borrower to make certain representations on the environmental condition of the property as part of the loan documentation. Most lenders also require provisions stating that, if the borrower becomes aware of any environmental problem after the loan date, the borrower will then notify the lender and provide it with copies of any reports and studies on the problem that the borrower has prepared.

© The Regents of the University of California

§7.92 2. Assurances on Remediation

Some years ago lenders would not even consider making loans on properties that were affected by contamination, but they are often more willing to do so today if the extent of the contamination and the expected cost of remediation has been well established and if the lender is comfortable with the parties' ability to complete and pay for the remediation. Because groundwater contamination takes longer to remediate and can also migrate, lenders may be more likely to provide financing for a property affected solely by soil contamination than one that is also affected by groundwater contamination. If the soil contamination can be remediated quickly and efficiently, however, the lender may require remediation before it will lend the funds.

In either circumstance, if the lender decides to fund the purchase, it will want assurances that the remediation will be completed. If the seller will be responsible for remediation after closing, the lender will probably require the same sort of assurances that the buyer requires of the seller. The lender may also seek a collateral assignment of the buyer's rights, if any, to require the seller to perform remediation, or else the right to require the buyer to enforce the seller's obligations to remediate, or both. If the buyer agrees to undertake remediation in exchange for acquiring the property at a price that reflects the existence of the contamination and the buyer assumes the obligation to remediate or remove it, the lender will probably want assurances that the buyer will perform the remediation. In either situation, the lender will probably require indemnities, reserve accounts, and possibly third party guaranties to be assured that the party undertaking remediation completes it.

© The Regents of the University of California

§7.93 3. Right to Waive Security

The most important aspect of the statutory enhancements of lenders' rights discussed in §7.90 is the material change to the antideficiency and one-action rules. These rules previously put a lender at risk because, if a property's value was impaired by contamination, a foreclosing lender would not be able to obtain a deficiency judgment (CCP §§580b, 580d) yet was required to foreclose on the property as the first effort to recover on a defaulted loan (CCP §726).

Now, under CCP §726.5, a lender may waive its security and proceed as if it held an unsecured loan if the real property collateral has been environmentally impaired and the borrower caused or permitted the contamination, or failed to disclose known contamination to the lender for loans, extensions of credit, guaranties, or other obligations made, renewed, or modified on or after January 1, 1992. A property will be considered environmentally impaired if a court confirms that the remediation or removal costs would exceed 25 percent of the fair market value of the property (without regard to the contamination) or the value of all security for the loan, whichever is greater, or if the property is the only parcel securing the loan and is listed on the National Priorities List under 42 USC §9605 or as a seriously contaminated property by the California Department of Health Services. CCP §736. For further discussion of the lender's ability to waive the security, see California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 4 (4th ed Cal CEB 2009).

© The Regents of the University of California

§7.94 4. Access, Right to Remediate, and Receivership

As a result of the provisions of the Civil Code and the Code of Civil Procedure that became effective January 1, 1992, lenders' documents often provide for (1) a lender's right of entry and inspection when foreclosure has commenced or the lender has a reasonable belief that toxic contamination has occurred (see CC §2929.5) and (2) a lender's right to perform remediation and appoint a receiver in connection with its performance (see CCP §564).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/7 Hazardous Waste Considerations/§7.95 5. Survival of Indemnities and Other Agreements After Foreclosure

§7.95 5. Survival of Indemnities and Other Agreements After Foreclosure

A lender may bring a separate action against a borrower for breach of any environmental provision regarding real property security, and such an action will not constitute an action under CCP §726 or a deficiency judgment that would otherwise be barred by CCP §580a, §580b, or §580d. CCP §736. This permits lenders to bring actions to address environmental problems without proceeding against the property by foreclosure or to recover further damages for environmental problems after a foreclosure. CCP §736(a).

Under CCP §736(b), damages are limited to the following:

- The reasonable cost of remediation or removal of contamination;
- Indemnity for third party claims relating to the contamination, as long as they arise from acts or omissions of parties, other than the lender, occurring while the borrower is still the owner or operator of the property; and
- Attorney fees and costs related to the breach.

Damages specifically available do not include principal and accrued interest or amounts attributable to contamination caused or knowingly permitted by the lender or its agents or affiliates. CCP §736(b). No benefit is derived from §736 for loans that are under $200,000 and meet other criteria set forth in CCP §736(c).

A more extensive discussion of the risks and benefits to lenders of different types of indemnities is beyond the scope of this book. Buyers and sellers of real property should, however, be generally aware of these different issues as they draft documentation for the purchase and sale of the property and enter into the loan application and documentation phases of the transaction. For further discussion of environmental indemnities, see California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 4 (4th ed Cal CEB 2009).

© The Regents of the University of California

8

Options, Rights of First Refusal, Puts, and Similar Rights

Nolan M. Kennedy
Thomas H. Jamison
Gordon K. Eng

I. GENERAL PRINCIPLES
- A. Definition of Option §8.1
- B. Types of Options §8.2
- C. Options in the Residential Context §8.3
- D. Options as Two Agreements §8.4
  - 1. Unilateral Contract for Right to Purchase §8.5
  - 2. Bilateral Contract for Purchase and Sale §8.6
  - 3. Additional Provisions in Option Contracts §8.7

II. CREATION OF OPTION CONTRACT §8.8
- A. Essential Elements of an Option Contract
  - 1. Essential Terms §8.9
  - 2. Consideration for Option §8.10
    - a. Adequacy of Consideration §8.11
    - b. Consideration for Options Within Other Agreements §8.12
    - c. Consideration Other Than Money §8.13
  - 3. Definiteness §8.14
  - 4. Statute of Frauds §8.15
  - 5. Term of Option and Rule Against Perpetuities §8.16
  - 6. Special Notices Required for Option Agreements §8.17
- B. Recording Option Contracts; Priority Issues §8.18
- C. Title Insurance for Option Contracts §8.19

III. EXERCISE OF OPTION
  - 1. Method of Exercise §8.20
  - 2. Time to Exercise §8.21
  - 3. Priority of Option on Exercise §8.22
  - 4. Waiver of Defective Exercise §8.23
  - 5. Changed Terms, Added Conditions, or Termination of Option After Exercise §8.24

IV. TRANSFER AND TERMINATION OF OPTIONS
- A. Transferability of Options
  - 1. When Option Is Assignable §8.25
  - 2. Transfer of Property Subject to Option §8.26
  - 3. Death of Optionor or Optionee §8.27
- B. Effect of Bankruptcy §8.28
- C. Condemnation and Destruction
  - 1. Condemnation §8.29
  - 2. Destruction §8.30
  - 3. Effect on Optioned Property §8.31
- D. Termination §8.32

V. ENFORCEMENT AND REMEDIES §8.33

VI. TAX CONSIDERATIONS §8.34
- A. Income Tax Treatment of Option Payment
  - 1. Optionor §8.35
  - 2. Optionee §8.36
- B. Tax Implication of Transfer of Option Right §8.37

VII. ADVANTAGES AND DISADVANTAGES FOR OPTIONOR AND OPTIONEE §8.38
A. Substitute for Liquidated Damages §8.39
B. Tax Deferral §8.40
C. Inducement to Investigate §8.41
D. Risk of Better Price §8.42
E. Uncertainty of Sale §8.43

VIII. USES OF OPTIONS §8.44
A. Land Acquisition and Land Use Development §8.45
1. Investigating Property §8.46
2. Processing Land Use Applications §8.47
3. Purchase Price §8.48
B. Obtaining Financing §8.49
C. Speculating on Value Increase §8.50
D. Assembling Multiple Parcels §8.51
E. Positioning for an Exchange Transaction §8.52
F. "Put" in Favor of Seller §8.53
G. Option as Financing Device §8.54
H. Convertible Mortgages §8.55
I. Joint Ownership Agreements §8.56
J. Options to Purchase in Lease §8.57
K. Right of First Refusal; Right of First Offer §8.58

IX. FORM OF OPTION AGREEMENT
A. Form: Introduction; Parties; Recitals §8.59
B. Form: Grant of Option §8.60
C. Form: Term of Option §8.61
D. Form: Consideration §8.62
E. Form: Successive Payments to Extend Option Term §8.63
F. Form: Exercise of Option §8.64
G. Form: Sequential Exercise of Option §8.65
H. Form: Covenants and Warranties of Optionor Concerning Property §8.66
I. Form: Condition of Title §8.67
J. Form: Investigation of Property §8.68
K. Form: Governmental Permits §8.69
L. Form: Assignment of Option §8.70
M. Form: Risk of Loss §8.71
N. Form: Condemnation §8.72
O. Form: Memorandum of Option to be Recorded §8.73
P. Form: Broker's Commission §8.74
Q. Form: Time of Essence; Failure to Exercise §8.75
R. Form: Attorney Fees §8.76
S. Form: Notices §8.77
T. Form: Entire Agreement §8.78
U. Form: Waiver §8.79
V. Form: Captions; Signatures §8.80
W. Form: Memorandum of Option §8.81
X. Form: Right of First Offer Agreement §8.82
Y. Form: Right of First Refusal Agreement §8.83

© The Regents of the University of California

I. GENERAL PRINCIPLES

§8.1 A. Definition of Option

An option contract is an irrevocable unilateral contract by one party (the optionor) to buy property from or sell property to another party (the optionee). *County of San Diego v Miller* (1975) 13 C3d 684, 688, 119 CR 491. When the option is exercised, a bilateral agreement is created for the purchase and sale of the property on the specified terms and conditions contained in the contract. *Jenkins v Tuneup Masters* (1987) 190 CA3d 1, 7, 235 CR 214; *Hudson Props. Co. v Governing Bd.* (1985) 168 CA3d 63, 72, 213 CR 909. An option itself does not transfer an interest in property. Rather, it is a grant of a right to purchase (or sell) the property. *Claremont Terrace Homeowners' Ass'n v U.S*. (1983) 146 CA3d 398, 406, 194 CR 216.

Option contracts are subject to the same customary rules of construction as other contracts. See, *e.g., Goodwest Rubber Corp. v Munoz* (1985) 170 CA3d 919, 216 CR 604; *Erich v Granoff* (1980) 109 CA3d 920, 167 CR 538. To be enforceable, an option contract must involve adequate consideration and must contain the material terms of the agreement. See §§8.9-8.13. Option contracts relating to the purchase and sale of real property fall within the statute of frauds and therefore must be in writing. See §§4.13, 8.15.

© The Regents of the University of California

§8.2 B. Types of Options

An option contract can take the form of a separate agreement entered into between the parties or can be part of another agreement between the parties, such as a lease. Common relationships between the parties to an option contract include:

- **Basic purchase option:** Seller makes an irrevocable offer to sell property to the buyer and the buyer may elect to accept and exercise its option at its discretion (see §§8.8-8.17);
- **Right of first refusal:** Buyer is given the right to buy property on the same terms as a third party offer received by the seller (see §8.58); and
- **Put:** Buyer makes an irrevocable offer to purchase the property that seller may elect to accept in its discretion (see §8.53).

Options outside the real estate context, most frequently in the corporate context, are not covered in this chapter.

© The Regents of the University of California

§8.3 C. Options in the Residential Context

In the residential context, the characterization of a contract as an option rather than a purchase agreement may have important consequences. In *Allen v Smith* (2002) 94 CA4th 1270, 114 CR2d 898, the buyer breached and the seller attempted to retain the entire deposit as the price paid for an option. The court, however, characterized the contract as a purchase and sale agreement instead of an option agreement. As a result, the court found that the seller was limited to the liquidated damages provided for in the contract rather than the entire deposit made on entering the contract.

When entering into residential option contracts, the parties must also consider compliance with the applicable statutory disclosure requirements. Although the option aspect of the option agreement may not invoke any disclosure obligations, the purchase and sale aspect of the option contract should be approached as any other residential purchase agreement. For a discussion of required disclosures in a residential purchase agreement, see §§6.29-6.70.

© The Regents of the University of California

§8.4 D. Options as Two Agreements

The option contract anticipates the completion of two necessary agreements: (1) the unilateral and irrevocable grant by the optionor to the optionee of the right or obligation to purchase the property (see §8.5), and (2) the underlying agreement of purchase and sale containing the material terms and conditions, including mutual obligations, that the parties must perform to close the transaction (see §8.6). The second agreement is contingent on the exercise of the first.

© The Regents of the University of California

§8.5 1. Unilateral Contract for Right to Purchase

As noted in §8.4, the first agreement in an option contract is a unilateral contract. *County of San Diego v Miller* (1975) 13 C3d 684, 119 CR 491; *Riverside Fence Co. v Novak* (1969) 273 CA2d 656, 660, 78 CR 536. One party (the optionee) gives consideration in exchange for the optionor's binding and enforceable promise to sell the property to or buy the property from the optionee; the consideration given can be either monetary or nonmonetary. See §§8.10-8.13. *City of Turlock v Paul M. Zagaris, Inc*. (1989) 209 CA3d 189, 194, 256 CR 902; *Erich v Granoff* (1980) 109 CA3d 920, 927, 167 CR 538. The optionor's binding and enforceable promise to sell (or buy) the property is a unilateral offer. As such, the optionee (the offeree) is commonly said to have exercised its option when it decides to accept the offer. In an option contract, the optionee is under no obligation to purchase (or sell) the property unless the option is exercised. *T.M. Cobb Co. v Superior Court* (1984) 36 C3d 273, 282, 204 CR 143, citing *Warner Bros. Pictures v Brodel* (1948) 31 C2d 766, 771, 192 P2d 949.

© The Regents of the University of California

§8.6 2. Bilateral Contract for Purchase and Sale

Once the unilateral contract (see §8.5) is accepted by the optionee (*i.e.,* the option is exercised), the option contract is converted into a bilateral contract for the purchase and sale of the property, with binding obligations to be performed by both parties. *Claremont Terrace Homeowners' Ass'n v U.S*. (1983) 146 CA3d 398, 406, 194 CR 216; *Anthony v Enzler* (1976) 61 CA3d 872, 132 CR 553.

The second agreement (the bilateral agreement) contained in an option contract involves the establishment of the terms and conditions of the purchase and sale of the property; thus, it is advisable to devote the same care to the drafting of this aspect of the option contract as any other purchase and sale agreement. For this reason, some practitioners attach a form of purchase and sale agreement to the option contract. Some parties prefer to delay drafting detailed purchase and sale provisions in order to, *e.g.,* present the other side with a short document or save costs or time in the face of a purchase that is not yet certain. As a result of this approach, however, (1) the parties may be unable to close because the material terms of the purchase have not been set forth in sufficient detail, or (2) the client may be able to close but has not obtained the benefit of the representations, warranties, or covenants that otherwise would have been expected if a purchase and sale agreement had been negotiated at the outset.

© The Regents of the University of California

§8.7 3. Additional Provisions in Option Contracts

An option contract generally must contain the two agreements described in §§8.4-8.6. However, when using an option contract to purchase real property, it is often advisable to include a number of additional provisions. For example, if an optionee intends to conduct environmental testing or other physical inspections and testing at the property, the optionee may require optionor's cooperation and optionor may require evidence of adequate insurance before allowing optionee to conduct testing. See §8.68. The additional provisions that may be appropriate will depend on the particular goals of the option contract. See §§8.66-8.72.

Although these additional mutual agreements may be necessary or helpful to carry out the intent of the parties, counsel for the optionee should consider whether the added mutual agreements have altered the unilateral nature of the option, which may affect the optionee's ability to easily exercise the option. For example, if the optionee must undertake certain acts such as processing land use entitlements within a given time and to a given standard, the optionee may be unable to exercise the option if those conditions are not met. The attorney should also consider the potential liabilities that may be created as additional agreements are incorporated into the option contract. For example, by adding duties of cooperation or confidentiality, the parties may create potential independent liabilities if they fail to perform these obligations.

© The Regents of the University of California

§8.8 II. CREATION OF OPTION CONTRACT

Option contracts are subject to statutory and case law requirements. Further, as with purchase and sale agreements, certain transactions have additional requirements. See §§6.29-6.70.

© The Regents of the University of California

A. Essential Elements of an Option Contract

§8.9 1. Essential Terms

An option contract must contain all of the essential terms of the purchase. These terms must be set forth in sufficient detail so that a court can enforce them. (On essential terms in a purchase and sale agreement, see §§4.6-4.13.) These terms include the following:

- The names of the parties;
- The price;
- The duration of the option; and
- A description of the property.

Stockwell v Lindeman (1964) 229 CA2d 750, 40 CR 555, citing *King v Stanley* (1948) 32 C2d 584, 589, 197 P2d 321. The California Supreme Court rejected the method and time of payment terms required by *Stockwell* and *King,* as essential terms. See *Patel v Liebermensch* (2008) 45 C4th 344, 86 CR3d 366. See also *Sterling v Taylor* (2007) 40 C4th 757, 772, 55 CR3d 116.

The bulleted terms are the minimum required to create an enforceable contract for the purchase of real property. *Hennefer v Butcher* (1986) 182 CA3d 492, 501, 227 CR 318. A court may imply other terms using custom and intent of the parties. See *Patel*, 45 C4th at 351 (time of payment); CC §1657 (time for performance of an act).

© The Regents of the University of California

§8.10 2. Consideration for Option

For an option contract to be enforceable, legally sufficient consideration must be given by the optionee for its option to purchase (or sell). Without consideration, the option contract is not binding on either party. An option contract that is not supported by consideration may be considered a mere offer that may be revoked at any time before acceptance. *Torlai v Lee* (1969) 270 CA2d 854, 76 CR 239. For a more detailed discussion on consideration in general, see §4.11.

© The Regents of the University of California

§8.11 a. Adequacy of Consideration

California courts have consistently stated that any consideration, however small, is sufficient to support the enforceability of an option contract. *Kowal v Day* (1971) 20 CA3d 720, 98 CR 118 (use of a car); *Wheat v Morse* (1961) 197 CA2d 203, 17 CR 226 (payment of $1); *Stough v Hanson* (1941) 46 CA2d 504, 116 P2d 77 ($1 in cash); *Marsh v Lott* (1908) 8 CA 384, 97 P 163 (payment of 25 cents). The consideration, however, must actually be given. In one case where the option contract provided that the optionor was required to return the option payment if the optionee did not exercise the option, the court held that the option contract failed for lack of consideration. *Torlai v Lee* (1969) 270 CA2d 854, 858, 76 CR 239; but see *Kowal,* 20 CA3d at 728 (holding that the optionor's ability to hold the option payment was sufficient consideration).

A price for the option may or may not be drafted into the option contract; if not, courts have little trouble finding sufficient consideration. See, *e.g., Kowal v Day, supra* (use of automobile sufficient consideration to support option). Practitioners, however, should clearly draft consideration for the option and also focus attention on drafting separate consideration for the purchase of the property. Although consideration is adequate regardless of amount, the purchase price may affect the availability of a specific performance remedy for breach of an option contract. See §4.149. In evaluating whether specific performance should be granted in a claim for breach of an option contract, case law has not focused on the consideration given for the first part of the option contract (*i.e.,* the irrevocable offer to buy or sell the property; see §§8.4-8.5). See *Auslen v Johnson* (1953) 118 CA2d 319, 323, 257 P2d 664; *Polinsky v Vaughan* (1968) 268 CA2d 183, 73 CR 764.

PRACTICE TIP: To strengthen the specific performance remedy available in the event of a breach by the optionor, a prudent optionee should consider proposing an option payment provision that bears a reasonable relationship to the purchase price and the term of the option contract. In addition, a sophisticated optionor is likely to require a significant option payment, especially in an appreciating market.

A disproportionately large amount of consideration can result in the option contract being recharacterized as a hidden financing device. For a discussion of the use of an option as a financing device, see §8.54.

© The Regents of the University of California

§8.12 b. Consideration for Options Within Other Agreements

In the context of options contained in other agreements, such as a right of first refusal or right of first offer contained in a lease, general contract principles are applied (*e.g.,* a single consideration supporting multiple promises). *Alpha Beta Food Markets, Inc. v Retail Clerks Union* (1955) 45 C2d 764, 771, 291 P2d 433. In the lease context, the consideration supporting the lease can also support an option agreement contained within the lease. For a discussion regarding office leases with an option to purchase, see Office Leasing: Drafting and Negotiating the Lease §1.75 (Cal CEB 1996).

© The Regents of the University of California

§8.13 c. Consideration Other Than Money

Traditional contract law rules apply to determine the adequacy of consideration for making a binding contract; thus, services or actions may also constitute valid consideration. The optionee needs to show that this consideration was bargained for and known to the optionor. *Kowal v Day* (1971) 20 CA3d 720, 726, 98 CR 118; *Kelley v Rouse* (1961) 188 CA2d 92, 10 CR 235; *Prather v Vasquez* (1958) 162 CA2d 198, 327 P2d 963. For example, the optionee may obtain valuable land use approvals for the property but if this work is not proven to be bargained-for consideration, and no other consideration is given, then the option contract may fail for lack of consideration. In addition, if the optionee is under no obligation to perform such work, then the option contract may also fail for lack of consideration. See *Steiner v Thexton* (review granted Sept. 17, 2008, S164928; superseded opinion at 163 CA4th 359, 77 CR3d 632) (optionee's obligation to deliver to optionor results of optionee's inspections of subject property was not sufficient consideration because optionee was under no obligation to perform such inspections). If the work improves the value of the property, however, the offeree may be able to recover the reasonable value of its services under CC §3343. See *Sixta v Ochsner* (1960) 187 CA2d 485, 9 CR 617.

© The Regents of the University of California

§8.14 3. Definiteness

If the essential terms of a contract are not sufficiently clear and definite, a court may refuse to enforce the contract. *Roberts v Adams* (1958) 164 CA2d 312, 320, 300 P2d 900 (option clause to purchase property for amount "payable as mutually agreed by both parties" is not sufficiently certain, and lessee's ability and offer to pay cash on exercise of lease's option did not cure uncertainty about terms of payment in option clause). Although courts occasionally interpret the language of a contract to make it more definite, the better practice is to make the provisions sufficiently definite. *Alameda Belt Line v City of Alameda* (2003) 113 CA4th 15, 18, 5 CR3d 879 (parol or extrinsic evidence can be used to explain meaning of ambiguous option terms, thus making them "sufficiently certain").

In the option portion of the option contract (*i.e.,* the unilateral contract described in §8.5), the description of the parties and of the property raises issues identical to those in a contract to purchase real property. See, *e.g., Malerbi & Assocs. v Seivert* (1961) 191 CA2d 760, 12 CR 852 (contract that failed to name the buyer-optionee was found inadequate). See §§4.6-4.7.

Every option contract contains two different price components: (1) the option price, and (2) the purchase price for the property subject to the option. When a formula or reference is used to determine the purchase price, rather than a fixed dollar amount, the formula or reference must be sufficiently clear. In *Goodwest Rubber Corp. v Munoz* (1985) 170 CA3d 919, 216 CR 604, the purchase price was defined as the "fair market value" of the property and the term of the option was 5 years. The court held that the exercise price was sufficiently clear to enforce the contract, siding with the optionee's view that setting a fixed purchase price for a date 5 years into the future was difficult.

PRACTICE TIP: Although the term "fair market value" is commonly used in the real estate industry, reasonable parties can disagree over the calculation of the actual dollars at issue. Detailed directions for calculating the purchase price can avoid this problem.

© The Regents of the University of California

§8.15 4. Statute of Frauds

An option contract that relates to the purchase of real property must satisfy the requirements of the statute of frauds. CC §1624(a)(3); *Woods v Bradford* (1967) 254 CA2d 501, 62 CR 391; *In re Watts* (Bankr ND Cal 2000) 244 BR 823. The contract or a memorandum of the contract must be in writing, and the writing must be signed by the party to be charged. On requirement of a writing, see §§4.12-4.13.

© The Regents of the University of California

§8.16 5. Term of Option and Rule Against Perpetuities

The length of the time within which an option may be exercised is an essential term in an option contract; otherwise, the contract violates the rule against perpetuities. If the term is omitted, however, the court may set a reasonable term, depending on the facts and circumstances of the case. *Southern Christian Leadership Conf. v Al Malaikah Auditorium Co.* (1991) 230 CA3d 207, 222, 281 CR 216; *Auslen v Johnson* (1953) 118 CA2d 319, 257 P2d 664.

California abolished the common law rule against perpetuities in 1991 in favor of a modified, statutory construction. Probate Code §21205 requires that an interest in real property vest either within the period of a life in being plus 21 years, or 90 years after creation. However, at the same time the legislature enacted the statutory rule against perpetuities, it also enacted Prob C §21225, which effectively exempts nondonative transfers from the rule. The rule against perpetuities does not apply to commercial, nondonative transfers, including options, preemptive rights of first refusal, future leases, and conditional leases. *Shaver v Clanton* (1994) 26 CA4th 568, 574, 31 CR2d 595. The rule against perpetuities applies to transfers rooted in family ownership, even if nondonative. Examples would include options granted under marital agreements, separation or divorce settlements, as consideration for a duty of support, and reciprocal transfers. Prob C §21225.

Even before 1991, only unusual situations triggered the rule against perpetuities. For example, in *Alamo Sch. Dist. v Jones* (1960) 182 CA2d 180, 6 CR 272, the court held that a right of first refusal that was effective only if the property was no longer used for school purposes violated the rule against perpetuities. See also *Strong v Theis* (1986) 187 CA3d 913, 232 CR 272; *Taormina Theosophical Community, Inc. v Silver* (1983) 140 CA3d 964, 190 CR 38.

NOTE: Practitioners should keep in mind that, apart from the options analysis, statutory law limits the duration of leases in certain circumstances. See, *e.g.*, CC §§715-719.

© The Regents of the University of California

§8.17 6. Special Notices Required for Option Agreements

In general, statutory notices that would be required in connection with a purchase and sale agreement for a given property will be required when an option agreement is entered into with respect to the property. Notices are required, for example, under CC §1102 (real estate transfer disclosure statements and mobilehome transfer disclosure statements), §1102.6(a) (additional requirements that may be established by local governments), §1102.6(b) (Mello-Roos Community Facilities Act special tax or assessment disclosures), §1103 (natural hazard disclosures). For a list of required notices, see §§6.29-6.70.

© The Regents of the University of California

§8.18 B. Recording Option Contracts; Priority Issues

Recording the option agreement or a memorandum of option in the real estate records in the county where the property is located establishes constructive notice to third parties of the option agreement. See *Thaler v Household Fin. Corp.* (2000) 80 CA4th 1093, 95 CR2d 779. When the optionee has no actual notice of a prior option agreement, the recordation would give the optionee priority over the prior option agreement. Moreover, any subsequent purchaser of the property would take subject to the recorded option. The recording of the option agreement or memorandum can defeat a claim by a purchaser or encumbrancer of property that it is a bona fide purchaser or encumbrancer who should take title free of the optionee's rights. See CC §1214.

Constructive notice of the existence of an option to purchase property expires either 6 months after the recorded instrument states the option expires by its terms or, if the instrument does not state a term, then 6 months after the recordation date of the instrument. CC §884.010.

Once the option is exercised, the title acquired by the optionee relates back to the date the option was granted. *Anthony v Enzler* (1976) 61 CA3d 872, 132 CR 553. The relation-back rule does not apply when the optionee obtains title to the property outside the purview of the option. If there is a failure of a condition, expiration of the option, or a material breach by the optionee that would preclude specific performance, the relation-back rule does not apply. *Wachovia Bank v Lifetime Indus.* (2006) 145 CA4th 1039, 52 CR3d 168.

© The Regents of the University of California

§8.19 C. Title Insurance for Option Contracts

Title insurance is available for option contracts. An optionee may want to insure the priority of the option right and the optionee's right to enforce the option or to insure that the optionor holds vested title to the property. Most title companies will issue insurance for an option in a form based on a standard owner's policy. See California Title Insurance Practice §§7.50-7.53 (2d ed Cal CEB 1997).

© The Regents of the University of California

III. EXERCISE OF OPTION

§8.20 1. Method of Exercise

If the option contract prescribes the method by which the option must be exercised, that method must be strictly followed. *Palo Alto Town & Country Village, Inc. v BBTC Co*. (1974) 11 C3d 494, 498, 113 CR 705; *Jenkins v Tuneup Masters* (1987) 190 CA3d 1, 7, 235 CR 214; *Riverside Fence Co. v Novak* (1969) 273 CA2d 656, 662, 78 CR 536. When the option contract does not specify the method by which the optionee can communicate its intention to exercise the option, any reasonable and customary method will be acceptable. *Palo Alto Town & Country Village, Inc.,* 11 C3d at 499; *Riverside Fence Co.,* 273 CA2d at 661. In California, under CC §1583 an option requiring written notice is exercised when the written acceptance is deposited in the mail. *Palo Alto Town & Country Village, Inc.,* 11 C3d at 501.

© The Regents of the University of California

§8.21 2. Time to Exercise

The exercise must be strictly within the time period specified in the contract. A late exercise of the option is generally not effective. See *Wachovia Bank v Lifetime Indus.* (2006) 145 CA4th 1039, 52 CR3d 168; *Allen v Smith* (2002) 94 CA4th 1270, 114 CR2d 898. However, courts have enforced a late exercise of an option when the delay was minor. See *Holiday Inns of Am. v Knight* (1969) 70 C2d 327, 74 CR 722 (court provided optionee relief from forfeiture).

Although the duration of an option is a material term, some courts have rescued the optionee by implying a reasonable duration. See *Bergin v Van Der Steen* (1951) 107 CA2d 8, 236 P2d 613 (agreement obligated optionor to allow additional time because contract language allowed for hiatus in obligation during war).

The language used to draft the duration can be fertile grounds for disagreement, which is why it is generally preferable, whenever possible, to identify a specific time and calendar date for an option's expiration. *Wilson v Gentile* (1992) 8 CA4th 759, 10 CR2d 713, is an example of how a court may interpret the duration provisions of an option agreement. In *Wilson*, the court construed an option to purchase requiring its exercise "within thirty days prior to the expiration of this option." A question arose about whether a fixed end point was established in the option language, *i.e.,* the date the option expired. The court determined that the beginning point of the time for lawful exercise of the option is defined as the given number of days before the end point. The interval between the beginning date and the ending date is the period "within" which the relevant event—in this case the exercise of the option—must occur.

In *Wilson*, the court distinguished between an option to buy and an option to renew a lease. In a lease renewal, the *Wilson* court felt it would be absurd to require the landlord to wait until the very end of the term to know whether the tenant was going to stay. The *Wilson* court, in the lease renewal situation, would be willing to substitute the words "at least" for the word "within." 8 CA4th at 765. See also 12 Witkin, Summary of California Law, *Real Property* §§533-534 (10th ed 2005).

The optionor cannot, however, evade or prevent actions that are required for the exercise of the option and then deny the effectiveness of an option that is otherwise timely exercised. *D-K Inv. Corp. v Sutter* (1971) 19 CA3d 537, 545, 96 CR 830; *Riverside Fence Co. v Novak* (1969) 273 CA2d 656, 663, 78 CR 536.

© The Regents of the University of California

§8.22 3. Priority of Option on Exercise

On exercise of the option, the bilateral contract to purchase and sell created by the exercise relates back in time to the moment the option was initially granted. *Claremont Terrace Homeowners' Ass'n v U.S*. (1983) 146 CA3d 398, 406, 194 CR 216. Because it relates back in time, when an option is properly exercised it has a right of priority over any encumbrance or other interest in the property that is acquired after the date of the initial grant of option. See *Marriage of Joaquin* (1987) 193 CA3d 1529, 1533, 239 CR 175 (property obtained through exercise of option during marriage is separate property if option created before marriage); *Claremont Terrace Homeowners' Ass'n v U.S., supra* (after exercise, option was transformed into an indefeasible right to acquire property which related back to date on which optionee first acquired option, which preceded recorded tax lien). That right of priority, like any other, can be defeated by a subsequent bona fide purchaser for value who acquires without actual or constructive notice of the option. *Gates Rubber Co. v Ulman* (1989) 214 CA3d 356, 364, 262 CR 630.

PRACTICE TIP: The optionee obtains important protection by recording a memorandum of the option. Recording can provide an optionee with priority over other option holders as well as purchasers of the property. See §§8.18, 8.81.

© The Regents of the University of California

§8.23 4. Waiver of Defective Exercise

In general, to be effective, the option must be exercised in strict accordance with its specified terms for acceptance. See §8.20. However, the optionor may waive the requirement of strict compliance. The waiver may be express or may be implied by the optionor's conduct.

EXAMPLE: The optionor may be deemed to have waived the defective exercise by not giving notice to the optionee, specifying the defects in the exercise of the option. *Rollins v Stokes* (1981) 123 CA3d 701, 713, 176 CR 835; *Collins v Marvel Land Co*. (1970) 13 CA3d 34, 40, 91 CR 291; *Riverside Fence Co. v Novak* (1969) 273 CA2d 656, 661, 78 CR 536.

© The Regents of the University of California

§8.24 5. Changed Terms, Added Conditions, or Termination of Option After Exercise

When the optionee purports to exercise the option but makes the exercise conditional in some way or changes the contract terms, the exercise of the option may be defective. In such a case, the classic rules of formation of contract apply to treat this as a counteroffer that rejects and thus terminates the original offer. See *State v Agostini* (1956) 139 CA2d 909, 912, 294 P2d 769 (acceptance of option must be unqualified and unconditional and according to terms of option).

Relief may be available, however, for an optionee who gives a conditional exercise of the option but withdraws these conditions before the option exercise period has expired. In *C. Robert Nattress & Assocs. v CIDCO* (1986) 184 CA3d 55, 229 CR 33, the court held that a conditional exercise was not a counteroffer that terminated the contract if not accepted. Rather, the conditions were considered additional terms that the optionor rejected. Because the conditional exercise did not terminate the option, the optionee was still able to accept the terms as stated in the option agreement.

In *McCulloch v M & C Beauty Colleges, Inc.* (1987) 194 CA3d 1338, 240 CR 189, a lessee had a right of first refusal (in effect an option; see §8.58) to purchase the property from its landlord. A third party made an offer to purchase the property and secure a note with a separate property. The lessee then exercised its option by making an identical offer but securing its note with different property. After the landlord sold to the third party, the lessee did not recognize the sale and refused to pay rent. The court held that the sale was valid because the value of the security for the note was of legitimate concern to the seller, as it was part of the consideration for the sale. The seller's decision regarding the sufficiency of the security is governed by the "reasonable person" standard. If the security is insufficient, the holder of a right of first refusal does not have automatic priority. 194 CA3d at 1346.

© The Regents of the University of California

IV. TRANSFER AND TERMINATION OF OPTIONS

A. Transferability of Options

§8.25 1. When Option Is Assignable

In general, option contracts are freely assignable. See *Mott v Cline* (1927) 200 C 434, 450, 253 P 718. However, parties are free to contractually prohibit or limit the ability to assign an option contract. In the absence of an agreement, courts have presumed an intent by the parties to prohibit an assignment when an assignee's performance would differ from the original party's performance. *Masterson v Sine* (1968) 68 C2d 222, 230, 65 CR 545. See also *Pritchard v Kimball* (1923) 190 C 757, 214 P 863 (court found option nontransferable when optionor entered into option agreement in reliance on financial position and credit record of optionee).

If the option is contained in a lease, an assignment of the lease will also assign the option in the absence of an express restriction on assignability of the option. *Maron v Howard* (1968) 258 CA2d 473, 484, 66 CR 70. In addition, the option may be separated from the lease and separately assigned if a prohibition of assignment is not expressed. *Spaulding v Yovino-Young* (1947) 30 C2d 138, 141, 180 P2d 691. If the lease has a clause that expressly prohibits assignment, that prohibition will also apply to separate assignment of the option. *Gatley v Shockley* (1932) 215 C 604, 611, 12 P2d 436.

© The Regents of the University of California

§8.26 2. Transfer of Property Subject to Option

The transfer of the option property does not in and of itself terminate the option contract. If the optionor owns the property, the option may be enforced against the transferee of the property if the transferee has actual or constructive (recordation of a memorandum of the option contract) notice or is otherwise not a bona fide purchaser. *Claremont Terrace Homeowners' Ass'n v U.S*. (1983) 146 CA3d 398, 406, 194 CR 216. The optionee also has traditional breach of contract remedies against the optionor.

© The Regents of the University of California

§8.27 3. Death of Optionor or Optionee

The death of the optionor does not affect the validity of the option. It remains enforceable against the deceased optionor's heirs or successors. *County of San Diego v Miller* (1975) 13 C3d 684, 688, 119 CR 491.

An option is also generally considered transferable on the death of the optionee, at which time it becomes an asset of the optionee's estate. See Prob C §9734; *Estate of Watts* (1984) 162 CA3d 1160, 1164, 208 CR 846. An option that by its terms is personal to the optionee, however, does not transfer on death; instead, it terminates. *Strong v Theis* (1986) 187 CA3d 913, 232 CR 272.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/8 Options, Rights of First Refusal, Puts, and Similar Rights/§8.28 B. Effect of Bankruptcy

§8.28 B. Effect of Bankruptcy

If the optionor files a petition in bankruptcy before the optionee exercises the option, exercise will be automatically stayed pending further action of the bankruptcy court. 11 USC §362(a). Further, the trustee has the power to assume or reject an executory contract of the debtor, subject to the bankruptcy court's approval. 11 USC §365(a). In the bankruptcy context, therefore, it can be important to ascertain whether a paid for but unexercised option is, in fact, executory.

An executory contract is one "on which performance remains due to some extent on both sides." *Unsecured Creditors' Comm. of Robert L. Helms Constr. & Dev. Co. v Southmark Corp. (In re Robert L. Helms Constr. & Dev. Co.)* (9th Cir 1998) 139 F3d 702, 705 (quoting *NLRB v Bildisco & Bildisco* (1984) 465 US 513, 522 n6, 79 L Ed 2d 482, 104 S Ct 1188). In *Helms,* the Ninth Circuit disapproved earlier cases holding that option contracts are by their nature executory and determined that whether a purchase option is executory depends on the particular characteristics of the option. The test is whether, at the time the bankruptcy petition is filed, the option requires that each party take some further action to avoid materially breaching the contract. If the answer is no, the option is not executory. The *Helms* court suggested that most options should not be considered executory, because the optionee typically does not commit a breach by doing nothing, *i.e.,* by permitting the option to expire. This may or may not be the case. Most option agreements do impose continuing obligations on the optionee, such as the obligation to indemnify the optionor if the optionee's entry on the property causes damage to the property. Whether these types of obligations are sufficient to render the option agreement executory will depend on whether the optionee's obligations are sufficiently material that the optionee's failure to perform them would excuse the optionor's performance under the option agreement. Thus, when the optionee has announced that the option will be exercised but has not followed through with the purchase at the option price, the option may be executory. 139 F3d at 706.

In the final analysis, whether the option agreement is or is not executory may not be critical in terms of completing the sale of the property. If it is not executory, the result is simply that the optionee is permitted, with court authorization, to exercise the option, and a bilateral executory agreement is created between the optionor, as seller, and the optionee, as purchaser. This does not put the optionee in a significantly better position than when a debtor optionee has exercised the option before filing a bankruptcy petition. In that event, the Bankruptcy Code treats the contract as a real estate purchase contract and applies executory contract principles. Thus, when appropriate, the trustee of an optionee who is a debtor in bankruptcy may accept (assume) or reject the contract following the prepetition exercise of the option. *In re Carlisle Homes, Inc*. (Bankr D NJ 1988) 103 BR 524. Court approval is required for the debtor either to reject or assume an executory contract. *Maroon v Four Star Pizza, Inc. (In re Four Star Pizza, Inc.)* (Bankr WD Pa 1992) 135 BR 498, 501; *Paul Harris Stores, Inc. v Mabel L. Salter Realty Trust (In re Paul Harris Stores, Inc.)* (Bankr SD Ind 1992) 148 BR 307, 313.

However, if the agreed purchase price for the property is below market value, the optionee has great incentive to prevail upon the court to hold that the purchase option is not executory so that the optionee can obtain the property. If the purchase option is held executory then it may be rejected by the debtor optionor. Rejection of a debtor's executory contract is deemed a breach of that contract, occurring immediately before the petition date. 11 USC §365(g). The nonbreaching party, the optionee in this case, is entitled to a claim for damages under contract principles when an executory contract is rejected in bankruptcy. *In re Aesthetic Specialties, Inc.* (Bankr 9th Cir 1984) 37 BR 679. Typically, this will be a general unsecured claim, treated pro rata with all other prepetition general unsecured claims against the debtor. As in many bankruptcy cases, the general unsecured debtor will not be paid the full amount of its claim, so the optionee would likely lose the full economic benefit of the purchase option.

In the case of an optionor-debtor, the optionee can try to protect itself against the optionor's bankruptcy by securing the optionor's obligations under the option agreement, and under the agreement of purchase and sale that would exist on exercise, by the lien of a deed of trust on the property. Such a deed of trust would list as the secured obligations not only the optionor's obligations under the option agreement and any resulting purchase agreement, but also any monetary damages resulting from the optionor's default under either agreement. Although such an arrangement might

be challenged as void under ipso facto principles, the optionee can argue that the security arrangement is effective for any breach of the applicable agreements, not only a breach in a bankruptcy context. Of course, any such deed of trust would generally have to be given with the consent of any existing secured lender, and such a lender may be hesitant to agree to the recording of such a deed of trust, even with strong intercreditor protections.

For further discussion, see Cherkis, Collier Real Estate Transactions and the Bankruptcy Code §4.02 (1992).

PRACTICE TIP: Another method of protecting against a bankruptcy by the optionor is to structure the ownership of the property so that it is held in a single-purpose bankruptcy-remote entity. If the property is the only asset of such an entity and the entity is not allowed to guarantee or otherwise stand behind any debts or other obligations that do not relate to the property, there is a better chance that the property will not be subject to bankruptcy. The optionor, however, may not be inclined to restructure its ownership of the property to achieve this added protection.

© The Regents of the University of California

C. Condemnation and Destruction

§8.29 1. Condemnation

If property that is subject to an option is condemned before the option is exercised and the option agreement does not otherwise address the issue, the optionee may receive that portion of the condemnation award that is in excess of the option purchase price. *County of San Diego v Miller* (1975) 13 C3d 684, 119 CR 491. When the option expires before the condemnation action is filed, however, the optionee has no compensable interest. *County of San Diego v Miller* (1980) 102 CA3d 424, 162 CR 480; *City of Walnut Creek v Leadership Hous. Sys*. (1977) 73 CA3d 611, 140 CR 690. For a discussion regarding valuing condemned property, see California Land Use Practice §21.113 (Cal CEB 2006).

A right of first refusal is similar to an option to purchase, which does not ripen until the owner of the property voluntarily decides to sell the property and receives a bona fide offer to purchase it from a third party. See §8.58. Condemnation for public need constitutes an involuntary taking and preempts a private party's preexisting right of first refusal to purchase. *Campbell v Alger* (1999) 71 CA4th 200, 83 CR2d 696 (county flood control district's condemnation of property for flood control purpose did not trigger private right of first refusal).

© The Regents of the University of California

§8.30 2. Destruction

Unless the parties specifically agree otherwise, the destruction of real property that is subject to a purchase and sale contract is governed by the Uniform Vendor and Purchaser Risk Act (CC §1662). See §§13.3-13.14. Although there have been no reported cases in California that have considered the effect of destruction of property subject to a purchase option before the option is exercised, it seems likely that the Act would apply, allowing the optionee to recover the option payment when the optionee did not cause the destruction and had not taken possession.

Although the California courts have not expressly considered the effect of a casualty on property subject to an unexercised purchase option, one case did examine the effect of the destruction of real property subject to a tenant's option to extend the lease term. In *11382 Beach Partnership v Libaw* (1999) 70 CA4th 212, 82 CR2d 533, the parties could terminate the lease if, during the last 2 years of the original term, the premises suffered damage that could not be repaired within 30 working days. The property was destroyed by fire less than 2 years before the expiration of the original lease term; immediately after the fire, the tenant exercised the option to extend the lease term, but the landlord terminated the lease. The court held that the tenant's option rights did not cut off the landlord's existing contractual right to terminate and that termination under such circumstances provides no basis for applying the rule against forfeiture.

PRACTICE TIP: Because the reasoning of the *Beach* case appears to apply to purchase options as well, counsel should keep these issues in mind when negotiating the casualty and condemnation provisions in a purchase option agreement.

© The Regents of the University of California

§8.31 3. Effect on Optioned Property

The effect of condemnation and destruction on real property subject to an option is uncertain. Because of this uncertainty in the law, the parties should specifically address these issues in the option contract. See §§8.71-8.72. What the parties provide with respect to condemnation and destruction during the period before the option is exercised may well differ from their agreement for the period after its exercise. The concerns are distinct, and their relative importance to the parties often varies, depending on whether the option is exercised or on other issues related to the contract. Thus, counsel should consider carefully the effect that either destruction or condemnation might have before and after exercise of the option and also consider the parties' ensuing insurance needs.

© The Regents of the University of California

§8.32 D. Termination

An option to purchase real property will terminate if not exercised within the time period set forth in the option agreement. *Rosenaur v Pacelli* (1959) 174 CA2d 673, 676, 345 P2d 102. On termination, the optionee has no further interest in the property. See *City of Walnut Creek v Leadership Hous. Sys*. (1977) 73 CA3d 611, 140 CR 690.

However, an option granted by two cotenants was not terminated when one of them subsequently sold his cotenancy interest to the optionee before the option term expired. The option continued in effect between the optionee and the remaining cotenant with respect to the remaining cotenant's interest in the property. *Penasquitos, Inc. v Holladay* (1972) 27 CA3d 356, 103 CR 717.

© The Regents of the University of California

§8.33 V. ENFORCEMENT AND REMEDIES

Typically, an option contract raises the same enforcement and remedy issues that arise in real property purchase and sale contracts, including damages and specific performance. The discussion of such issues in §§4.140-4.150 is applicable.

Two situations are peculiar to the option contract. They arise when (1) the optionor wrongly repudiates the option contract, and when (2) the optionee chooses not to exercise the option and brings suit based on the unilateral contract for the option instead of the bilateral contract for the purchase and sale.

In *Schmidt v Beckelman* (1960) 187 CA2d 462, 9 CR 736, the optionor wrongly repudiated the option, and the optionee sued for damages but never exercised the option. The court held that the proper measure of damages was the actual damage incurred by the optionee, which would at least include the difference between the amount paid for the option and its actual value. The court rejected the trial court's application of CC §3306 to establish damages as the difference between the property's purchase price and its fair market value. 187 CA2d at 471.

In *Holiday Inns of Am., Inc. v Knight* (1969) 70 C2d 327, 74 CR 722, the optionor wrongly repudiated an option in the fourth year of its 5-year term while the optionee was developing adjacent land and apparently not ready to exercise the option. The optionee sued for and obtained a declaratory judgment that the option contract was still effective.

NOTE: The option expired before the supreme court's opinion reversing the trial court and ordering entry of declaratory judgment that the option was effective. The supreme court did not address the issue of whether the option could still be exercised.

© The Regents of the University of California

§8.34 VI. TAX CONSIDERATIONS

Tax issues are an inescapable aspect of every real property transaction. It is essential to consider the federal and state income tax implications for both the optionor and the optionee. The following is a general discussion of the basic tax principles that apply in most real property option contracts. For a more detailed discussion of the tax treatment of options, see 2 Bittker & Lokken, Federal Taxation of Income, Estates and Gifts ¶¶40.8.3, 57.3 (3d ed 1999); Robinson, Federal Income Taxation of Real Estate ¶12.06 (6th ed 1995).

© The Regents of the University of California

A. Income Tax Treatment of Option Payment

§8.35 1. Optionor

Generally, payments to acquire options are not taxable to the optionor when received. Although some early authorities (and some commentators) suggest that option payments that are not applied against the purchase price of the property on exercise of the option are immediately taxable (*Virginia Iron, Coal & Coke Co. v Commissioner* (4th Cir 1938) 99 F2d 919; Augustine & Zarrow, California Real Estate Law and Practice §70.53[1]-[2]), that rule is not generally followed by more recent authorities and is not endorsed by most commentators (see *Johnie Vaden Elrod* (1986) 87 TC 1046, 1067; *Carl E. Koch* (1976) 67 TC 71, acq 1980 Cum Bull 1; Robinson, Federal Income Taxation of Real Estate ¶12.06 (6th ed 1995); 2 Bittker & Lokken, Federal Taxation of Income, Estates and Gifts ¶40.8.3 (3d ed 1999). If the option is exercised, the option payments are included in the optionor's amount realized for the property for the purpose of determining the optionor's gain or loss on the sale. If the optionee does not exercise the option, the option price is taxable to the optionor as ordinary income on the date the option expires. Robinson, Taxation of Real Estate ¶12.06.

In some cases, the Internal Revenue Service may take the position that amounts called "option payments" by the taxpayer should be recharacterized. For example, the IRS may claim that option payments made by a lessee or licensee are, in whole or in part, rent or royalty payments (see, *e.g., Commissioner v Dill* (3d Cir 1961) 294 F2d 291), or that option payments are wholly or partly interest on an installment sale of the property (see, *e.g., Carl E. Koch, supra*). If the IRS were successful in such a recharacterization, the taxation of the option payment would depend on its true nature.

Care should be taken when payments related to the option agreement are to be made over a course of years, because the option agreement may be considered an installment sale. IRC §453. If the agreement is considered an installment sale, the option payments are considered income when received. To avoid installment sale treatment, a single payment for the option is advisable, but in some cases the parties may want a series of payments. In such instances, the parties may want to provide that the payments are not applicable to the purchase price.

© The Regents of the University of California

§8.36 2. Optionee

The option consideration is treated by the optionee as part of the purchase price, if the option is exercised, and is added to the basis of the property even if it is not applied to the purchase price. *C.H. Mead Coal Co. v Commissioner* (4th Cir 1934) 72 F2d 22. If the option lapses, the optionee is treated as having a loss in the amount of the option payments made from the sale of the option occurring on the date the option expires. IRC §1234(a)(2). In that case, the loss will be capital or ordinary depending on the character the property would have had in the hands of the optionee if it had been acquired, and, if capital, will be short- or long-term depending on the optionee's holding period for the option. Treas Reg §1.1234-1(a).

© The Regents of the University of California

§8.37 B. Tax Implication of Transfer of Option Right

The optionee's transfer of the option right results in a taxable gain or loss to the optionee that has the same character as the property to which the option relates would have had if it were owned by the optionee. IRC §1234(a)(1). Thus, the transfer of an option in real property that would be capital gain property in the hands of the optionee will produce a capital gain or loss to the optionee on the transfer.

© The Regents of the University of California

§8.38 VII. ADVANTAGES AND DISADVANTAGES FOR OPTIONOR AND OPTIONEE

Generally, options are considered to be most favorable to optionees, whose only risk is the loss of the option price and any other investment in the transaction. The optionor incurs a greater risk, for which the option price is intended to compensate. The optionor should not consider the option price as "found" money but should seriously evaluate the detriment of the option as an element in establishing its price. An option does, however, have certain benefits to an optionor. See §§8.39-8.41.

© The Regents of the University of California

§8.39 A. Substitute for Liquidated Damages

Many sellers prefer to structure their dispositions of real estate as options because they believe that the consideration for the granting of the option would provide a more certain claim to the money than an action for breach of contract or to enforce a liquidated damages provision. Payment of the option price may avoid the issue for the seller of whether retention of the deposit is enforceable as liquidated damages. Many sellers using the option consideration approach, however, include a "protective liquidated damages provision," stating that if the option consideration is held to be liquidated damages, then those liquidated damages are enforceable as such. This provision must comply with CC §§1671-1681. Counsel should note, however, that an unreasonably high option price may cause the transaction to be recharacterized as a purchase agreement with a deposit so large as to cause an unreasonable forfeiture if the transaction is not consummated. See, *e.g., Scarbery v Bill Patch Land & Water Co*. (1960) 184 CA2d 87, 7 CR 408.

For tax purposes, an option payment that is too high in relation to the ultimate purchase price may cause the transaction to be recharacterized as an installment sale, with periodic option payments treated as interest on an installment note. See *Johnie Vaden Elrod* (1986) 87 TC 1046; Rev Rul 82-150, 1982-2 Cum Bull 110.

© The Regents of the University of California

§8.40 B. Tax Deferral

The option payment is generally not taxable to the optionor until the option is exercised. See §8.35. The opportunity for a tax deferral is often desirable to sellers.

© The Regents of the University of California

§8.41 C. Inducement to Investigate

Sellers of real property try to minimize their obligations of disclosure and their warranties about the property. See §§1.70-1.93. One way to do this might be to give a prospective purchaser an option with the ability to fully investigate the property before exercising the option. This could allow the seller to effectively bargain for minimal disclosure and warranties, and can be a powerful inducement to the buyer to perform its due diligence.

© The Regents of the University of California

§8.42 D. Risk of Better Price

The principal risk to the optionor under an option contract is the potential increase in property value during the option period. Another potential buyer may even approach the optionor and offer a better price for the property during the option term. The optionee, however, has bought the optionor's commitment to sell at a fixed price and the price the optionee paid for the option is intended to compensate the optionor for this risk.

© The Regents of the University of California

§8.43 E. Uncertainty of Sale

The most obvious disadvantage to the optionor is that the optionee may choose not to exercise the option. In the meantime, the optionor's property has been tied up, drilling or other investigation activities may have been performed, land use applications may have been filed, or other opportunities for the property may have been missed. The optionor and the attorney should consider and address these issues in the option contract as specifically as possible in light of the particular circumstances of the property and the parties to the transaction.

© The Regents of the University of California

§8.44 VIII. USES OF OPTIONS

Options are used for many purposes. Some common and some more creative uses are discussed in §§8.44-8.58, together with some of the principal motivations for entering into an option contract instead of directly entering into a purchase and sale agreement.

© The Regents of the University of California

§8.45 A. Land Acquisition and Land Use Development

Option contracts are often used by developers who believe a particular property is suitable for development, but expect that it will take considerable time to verify the feasibility of acquiring and developing it. Option contracts are also often used by developers who wish to obtain land use approvals before committing to purchasing the property. Obtaining land use approvals can be expensive and time consuming in California, and a developer may have no interest in owning the property if land use approval cannot be obtained. A number of issues should be considered when using an option contract in these contexts.

© The Regents of the University of California

§8.46 1. Investigating Property

A developer-optionee will generally require access to the property to complete a feasibility review of the property, including an environmental review, soils testing, surveys, appraisals, and other investigations. See form 8.68-1 and §§4.46-4.49, 4.77-4.82. For a discussion of preliminary preparation steps in the land use permitting process, see California Land Use Practice §1.37 (Cal CEB 2006). In such cases it is common for the developer-optionee to require the owner-optionor to reasonably cooperate with such activities. However, an owner-optionor should consider obtaining protection from the developer-optionee against personal or property injuries that may arise in the course of developer-optionee's investigation. Further, the owner-optionor should obtain copies of any reports produced as a result of such investigations. With respect to property feasibility and investigation issues, the optionor and optionee have many of the same concerns as arise under a purchase and sale agreement. However, because the optionee has complete discretion to decide whether to exercise an option and proceed with the purchase, questions of good faith and satisfaction of conditions do not arise.

© The Regents of the University of California

§8.47 2. Processing Land Use Applications

In general, development of land in California, whether improved or unimproved, including changing its permitted uses, is subject to a variety of governmental approvals. A number of these governmental approvals are discretionary, which means that the applicable agency can deny a request or condition the issuance of its approval on the satisfaction of an increasingly complicated and time-consuming set of requirements that can take years to satisfy. See California Land Use Practice §§1.39-1.43 (Cal CEB 2006). Because a developer may have no interest in owning the property (and thus incurring all of the costs and obligations of ownership) if the required land use approvals cannot be obtained, an option on the property may suit the developer's goals.

As a mere optionee and not the property owner, the developer may lack the authority to enter into land use agreements with applicable government agencies. Accordingly, a developer may require the owner-optionor to sign documents to be submitted to government agencies that request land use approvals, or to take actions such as appearing at public hearings and speaking in favor of a project. The owner should be concerned about, and address any issues that arise from, allowing any land use action that will obligate the owner in the event the developer does not exercise the option and purchase the property. One way the property owner may protect itself is to require that any land use changes must be made final only after the property is sold to the developer.

© The Regents of the University of California

§8.48 3. Purchase Price

A property owner will not be inclined to enter into an option contract that will potentially tie up the property for years only to sell the property at the market price prevailing at the time the option agreement is signed. The lure presented by the developer to the owner is a purchase price above market price. The purchase price is thus a topic of negotiation, and the property owner and developer will need to speculate on the estimated future value of the property as well as the property owner's potential costs in tying up its property for the option period.

© The Regents of the University of California

§8.49 B. Obtaining Financing

Most properties are purchased with some amount of third party financing. To satisfy a lender, a potential borrower may be required to provide a substantial equity contribution or cure property conditions (*e.g.,* environmental contamination). These conditions may take considerable time to satisfy. An option contract can be used to obtain the necessary commitment by the owner to sell, and also provide time to satisfy the lender's conditions. Alternatively, a purchase agreement may provide for a financing contingency. See §4.83.

© The Regents of the University of California

§8.50 C. Speculating on Value Increase

Using an option contract solely to tie up property at the current market price in the hope that the value will increase is becoming increasingly rare. Optionors have previously entered into such agreements only with the expectation that the optionee would undertake improvements to the property to increase its value. In some cases, however, a landowner may allow the optionee to enter into an agreement without requiring improvements if it is satisfied with the receipt of the option payment.

© The Regents of the University of California

§8.51 D. Assembling Multiple Parcels

One risk a developer faces in assembling multiple parcels for a planned development is that the developer may not be able to acquire a key parcel. To minimize this risk, the developer can acquire options on the various parcels until the rights to every parcel needed for the development are obtained. An assemblage can present some unique problems. The developer may want to keep its goals quiet yet at the same time will likely have a desire to close on the entire assemblage once it has obtained appropriate financing and land use approvals. Some artful drafting may be required to coordinate the purchases and achieve these goals. For example, the developer may include confidentiality provisions in its options and may provide that the closing of the purchase is subject to conditions that would apply to all of the properties in the assemblage.

© The Regents of the University of California

§8.52 E. Positioning for an Exchange Transaction

As various means of tax deferral in real estate transactions have been restricted or eliminated, exchanges of like-kind property have become increasingly popular for tax deferral. One problem with an exchange is coordinating the timing so that the exchange property is available and the transaction can close as required to meet the requirements of IRC §1031. Although the advent and acceptability of deferred exchanges, including so-called reverse exchanges or parking transactions, have eased the pressure somewhat, the time limits for a deferred exchange still necessitate having the exchange property, or a potential buyer, available as early as possible. Many of the timing problems may be solved or at least minimized by using an option. For a discussion of the use of options in real property exchanges, see Real Property Exchanges §4.33 (3d ed Cal CEB 2002). See also §§1.101, 4.165.

© The Regents of the University of California

§8.53 F. "Put" in Favor of Seller

A seller may have an option to require a purchaser to buy property at a fixed price during a prescribed period of time. This situation may occur, for example, in a cotenancy agreement in which a deceased cotenant's estate has the option to "put" the property to the survivor, thus requiring the survivor to purchase the decedent's interest. Another use may arise when the parties want to complete a finished transaction for some reason (such as needing to meet timing requirements in an exchange), but the purchaser is uncertain about some element of the property. The seller then may give the purchaser the right to require the seller to repurchase the property. These are only two situations in which a "put" may be useful.

The considerations discussed in §§8.38-8.43 regarding the option agreement will be identical for a "put." An additional consideration that the holder of a "put" must take into account is that the other party must be in a position to close the transaction at all times during the option term. The holder of the "put" may require security, such as a letter of credit or an institutional financing commitment, to ensure the purchaser's continuing ability to perform.

In contrast to an option to purchase, the "put" must be supported by consideration running from the seller to the purchaser. If the seller does not give adequate consideration, the purchaser's obligation to buy is unenforceable. See §§8.10-8.13. *Dawson v Goff* (1954) 43 C2d 310, 273 P2d 1.

© The Regents of the University of California

§8.54 G. Option as Financing Device

What would otherwise be a loan secured by a deed of trust may be structured instead as a sale-leaseback that gives the seller-tenant an option to repurchase the property. If properly structured and documented, this form of transaction will be respected and may produce more satisfactory tax consequences for the parties. For a detailed discussion of sale-leasebacks and their tax consequences, see Maule, Taxation of Real Estate Transactions—An Overview, 590-2d BNA Tax Mgmt Portfolio A18-A19 (2005).

A seller-tenant-optionee who has an option to repurchase will sometimes contend that it is actually a security instrument and that the buyer-landlord-optionor is obligated to comply with antideficiency, foreclosure, or other rules applicable to real property loans and security instruments. See, *e.g., Develop-Amatic Eng'g v Republic Mortgage Co*. (1970) 12 CA3d 143, 91 CR 193. In general, courts look to the intent of the parties to determine whether the agreement should be deemed a security instrument. See *Beeler v American Trust Co*. (1944) 24 C2d 1, 23, 147 P2d 583; *Gronenschild v Ritzenthaler* (1947) 81 CA2d 138, 145, 183 P2d 720. The adverse aspect of an option agreement being deemed a security instrument is that the document probably was not drafted as a security instrument. For example, it will probably not contain a power-of-sale provision, which will limit the offeree to a suit for judicial foreclosure to acquire the property. A judicial foreclosure is likely to be more expensive and time consuming than a foreclosure by a power of sale. Additionally, a judicial foreclosure is subject to reinstatement and redemption protections for the offeror. See California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 3 (4th ed Cal CEB 2009).

© The Regents of the University of California

§8.55 H. Convertible Mortgages

An option may be used as part of a financing package by giving the lender an option to purchase all of the property or an interest in it. This practice may produce better loan terms for the borrowing developer while giving the lender an enhanced profit if the project is successful.

A traditional concern in such a transaction was whether it constituted a "clogging of the equity of redemption." That concern was eliminated in 1984 with the adoption of CC §2906. See *Wachovia Bank v Lifetime Indus.* (2006) 145 CA4th 1039, 1057, 52 CR3d 168. This section makes such transactions valid except those involving residential real property of four or fewer units or those in which the right to exercise the option depends on the occurrence of a default. For further discussion of convertible mortgages, see California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 1 (4th ed Cal CEB 2009).

Few institutional lenders have taken an option to acquire the subject collateral as one of the loan terms in a nondefault situation. Some institutional lenders would face regulatory difficulties in doing so (*e.g.,* national banks). It is more common for lenders to use a shared appreciation loan, which allows the lender to share in the subject collateral's operating cash flow or appreciation as an element of "additional interest." See*, e.g.*, CC §§1917-1917.006.

© The Regents of the University of California

§8.56 I. Joint Ownership Agreements

Most well-drafted agreements between co-owners of property contain one or more options. There may be an option to purchase on death, bankruptcy, or some other disruptive event. An option to purchase may be used as a mechanism for resolving disputes. The use of options for these purposes is discussed in more depth in Nellis & Murray, *Negotiating and Drafting a Real Estate Joint Venture Agreement: Major Issues and Provisions, Part II*, 12 CEB Real Prop L Rep 1 (Jan. 1989).

In these agreements, the principal issue will be the method of establishing the purchase price for the property. Another issue that should be addressed specifically in the contract—and that is atypical of an ordinary option agreement—is whether the option provisions will encumber or benefit a successor to one of the original parties to the agreement. See *Strong v Theis* (1986) 187 CA3d 913, 232 CR 272. See paragraph 12 of App O for a sample form.

© The Regents of the University of California

§8.57 J. Options to Purchase in Lease

When an option to purchase real property is included in a lease of the property, certain added considerations apply, as well as some modifications of the general option contract rules.

- No separate consideration for the option is required to make it enforceable if the option is part of a lease. The tenant's consideration in the lease in the form of rent is sufficient. *Spaulding v Yovino-Young* (1947) 30 C2d 138, 141, 180 P2d 691.
- When there is no separate consideration for the option, termination of the lease will also terminate the option. *Wallace v Imbertson* (1961) 197 CA2d 392, 17 CR 117.
- The rule against perpetuities probably does not apply to an option that is part of a lease, although California law is still unsettled on this issue. See §8.16.
- An assignment of a lease will also assign the option unless the option's assignment is specifically prohibited, and, conversely, the option may be assigned separately from the lease unless that too is specifically prohibited. See §8.25.
- If the lease is extended or renewed by an agreement or by an option right in the lease, the option to purchase will likewise be extended or renewed if that was the parties' intention. *Riverside Fence Co. v Novak* (1969) 273 CA2d 656, 78 CR 536. It is important in drafting the option contract to make the parties' intent clear.

An option to purchase in a lease is generally for a significantly longer term than is ordinarily the case in nonlease options. The option might not even become effective until some portion of the lease term has expired. Thus, the parties may be unable to establish the purchase price for the property at the time the lease is executed, and some mechanism such as a formula or appraisal may be necessary. On options to purchase, see Ground Lease Practice, chap 6 (2d ed Cal CEB 2009) and Office Leasing: Drafting and Negotiating the Lease §1.75 (Cal CEB 1996).

© The Regents of the University of California

§8.58 K. Right of First Refusal; Right of First Offer

Rights of first refusal and rights of first offer are alternative forms of option agreements. They must satisfy the same essential requirements as options, such as definiteness (see §8.14) and consideration (see §§8.10-8.13). However, some issues are particular to these types of option agreements.

A right of first refusal affords the optionee the right to match or better an offer to purchase received by the optionor. A right of first offer requires the optionor to offer to sell the property to the optionee before offering it to anyone else. A right of first offer allows the optionor to proceed to sell the property on the same or better terms if the optionee does not accept the optionor's offer.

In general, a right of first refusal is triggered by a proposed voluntary sale by the offeror. See *Pellandini v Valadao* (2003) 113 CA4th 1315, 7 CR3d 413. An involuntary condemnation of the property does not trigger the right of first refusal. See *Campbell v Alger* (1999) 71 CA4th 200, 83 CR2d 696.

In contrast to traditional option agreements, under a right of first refusal the optionee may not be in control of the terms and conditions set forth in the offer to purchase. In general, an optionee is not required to match exactly the offer to purchase received by optionor if the offer is of a nature that cannot be easily matched by anyone other than the offeror. Courts will consider commercial realities in evaluating whether the optionee has matched or bettered the offer to purchase. *Arden Group, Inc. v Burk* (1996) 45 CA4th 1409, 53 CR2d 492. See also *San Diego Watercrafts, Inc. v Wells Fargo Bank, N.A.* (2002) 102 CA4th 308, 125 CR2d 499; *McCulloch v M & C Beauty Colleges, Inc.* (1987) 194 CA3d 1338, 240 CR 189. But in *Hartzheim v Valley Land & Cattle Co.* (2007) 153 CA4th 383, 394 n6, 62 CR3d 815, the court seemed to imply in a footnote that because the optionee was unable to match the unique terms of the offer, the optionee could not have exercised its right of first refusal.

The mechanics of a right of first refusal or right of first offer must be addressed when drafting the agreement. The agreement should specify whether the option applies only to the first instance in which it can be exercised or whether it renews if the optionor does not successfully close the offer. For the offeree, it is useful to establish objective guidelines for the terms and conditions that the offer must follow so that there will be less room for disagreement as to whether offeree has matched such offer.

A right of first refusal is considered more likely to have an adverse, rather than favorable, effect on the price at which the offeror can sell the property. A prospective purchaser will be less inclined to spend the time and money to evaluate the property and negotiate a purchase agreement if the purchaser is aware that the offeree could step in under its right of first refusal and acquire the property by matching the purchaser's offer.

From an offeree's point of view, the right of first offer represents a way to validate the proposed purchase terms because an independent third party is willing to purchase the property on those terms. A right of first offer allows the offeror to market the property more easily after offering the property to the offeree. However, the offeror may not be sufficiently knowledgeable about the market value of the property to present an offer to the offeree. This deficiency can be addressed if the offeror consults brokers or appraisers or potential buyers before presenting the offer to offeree. From the offeree's point of view, the offeree may not have a sufficient basis to determine whether the offered price and terms reflect the current market.

The parties should consider including specific requirements for the terms and conditions of the right of first offer, such as requiring the purchase price to be all cash. If the offer is not limited to a cash purchase price it may be difficult for the offeree to match the offer.

In either a right of first refusal or a right of first offer, the offeror may want to limit the representations and warranties to be made to the offeree, as opposed to the third party purchaser, because the offeree is likely to be more knowledgeable about the property than a third party purchaser. Because the right of first offer is often part of another transaction, such as a lease, it may be appropriate to limit the assignment of this right, and the offeror should consider limiting the offeree's ability to transfer the right of first offer.

© The Regents of the University of California

IX. FORM OF OPTION AGREEMENT

§8.59 A. Form: Introduction; Parties; Recitals

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

8.59-1 Introduction; parties; recitals

Option Agreement

This Option Agreement is made between _ _[*name*]_ _ (Optionor) and _ _[*name*]_ _ (Optionee). This Option Agreement is dated _ _[*date*]_ _, for reference purposes only.

Comment: The issues of identifying the parties are identical to those discussed in the context of the purchase and sale contract. See §§4.7, 4.14-4.21, 4.29, 8.9. Dating the agreement for reference purposes only is a convenient way to ensure that the agreement date is not omitted. Signature dates can then be used on the signature page. See §8.80.

Recitals of relevant facts can follow the introductory paragraph. These recitals often help clarify the agreement by explaining background facts and can also serve as a place to establish important definitions (such as the property description) at the beginning of the document.

© The Regents of the University of California

§8.60 B. Form: Grant of Option

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

8.60-1 Grant of option

1. *Grant of Option.* Optionor grants to Optionee the option to purchase the real property described in the attached Exhibit _ _[*e.g., A*]_ _ (Property). This option is on the terms and conditions set forth in this Option Agreement. The purchase and sale of the Property on exercise of this option shall be on the terms and conditions set forth in the Purchase and Sale Agreement, attached as Exhibit _ _[*e.g., B*]_ _ (Purchase Agreement).

Comment: Because an adequate property description is an essential element of an option contract (see §8.9), it is good practice to make a legally sufficient description a part of the option contract. See §§11.14-11.41 for discussion of what constitutes a legally sufficient property description.

The ultimate agreement for purchase and sale can be attached as an exhibit as suggested by the form, or it can be made a part of the option contract. See §§4.166-4.182 for a form of the purchase and sale agreement.

© The Regents of the University of California

§8.61 C. Form: Term of Option

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

8.61-1 Term of option

2. *Term of Option.* The _ _[*initial*]_ _ term of the option shall begin on _ _[*date*]_ _, and shall terminate at _ _ _ a.m./p.m. (California time) on _ _[*date*]_ _.

[*If appropriate, add*]

As long as this Option Agreement remains in effect, Optionee may extend the term of the option for the periods described in _ _[*e.g., 3.2*]_ _ by timely payment of the extension payment amounts described in that section.

[*Continue*]

Comment: If successive option terms are part of the agreement (see clause in §8.63), the first paragraph of this provision should state that it is the "initial term." In addition, use the second paragraph if options to extend the term are granted.

© The Regents of the University of California

§8.62 D. Form: Consideration

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

8.62-1 Consideration

3. *Consideration.*

3.1. *Payment of Consideration.* On the execution and delivery of this Option Agreement, Optionee shall pay to Optionor, in immediately available funds, the sum of _ _[*dollar amount*]_ _ as consideration for the option. The option consideration set forth in this section, as well as any other consideration deemed to have been received by Optionor under this Option Agreement, is and shall be deemed consideration solely for the granting of the option by Optionor. On expiration of the option term, Optionor shall retain all option consideration. If the option is exercised, the consideration _ _[*shall/shall not*]_ _ be credited against the purchase price of the Property,

[*Add if consideration is to be applied to purchase price*]

if closing occurs in accordance with the Purchase Agreement.

Comment: The phrase "if closing occurs in accordance with the Purchase Agreement" is included to be certain that, if something has happened that changes the purchase agreement but the parties proceed to close, the price provisions will not be automatically applied without further review by the parties in light of the changed circumstances.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/8 Options, Rights of First Refusal, Puts, and Similar Rights/§8.63 E. Form: Successive Payments to Extend Option Term

§8.63 E. Form: Successive Payments to Extend Option Term

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

8.63-1 Successive payments to extend option term

[*If applicable, add the following option*]

[*Option: Optionee may extend term and make successive payments*]

3.2. *Successive Payments to Extend Option Term.* Optionee may extend the term of the option from the expiration of the Initial Term until _ _ _ a.m./p.m. (California time) on _ _[*date*]_ _ (First Extended Term), by payment to Optionor, in immediately available funds, the sum of _ _[*dollar amount*]_ _ on or before the _ _[*e.g., 14th*]_ _ day before the expiration of the Initial Term.

[*If appropriate, add*]

As long as Optionee has extended the term of the option for the First Extended Term, Optionee may extend the term of the option from the expiration of the First Extended Term until _ _ _ a.m./p.m. (California time) on _ _[*date*]_ _ (Second Extended Term), by payment to Optionor, in immediately available funds, the sum of _ _[*dollar amount*]_ _ on or before the _ _[*e.g., 14th*]_ _ day before expiration of the First Extended Term.

[*Continue*]

_ _[*All*]_ _ **Payments made under this section _ _ _ _ _[*shall/shall not*]_ _ be applied to the purchase price of the Property.**

[*Continue*]

Comment: This form should be used in conjunction with the form in §8.61 if options to extend the option term are granted. This form provides that the extension of the option term occurs on payment. The optionee should make sure that payment is accompanied by written notice specifying that the payment is in consideration of the extension.

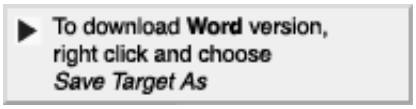
Additional extended terms (*e.g.,* Third Extended Term, Fourth Extended Term) may, of course, be added. The option agreement should address whether the additional option payments are to be applied against the purchase price.

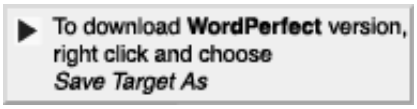
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/8 Options, Rights of First Refusal, Puts, and Similar Rights/§8.64 F. Form: Exercise of Option

§8.64 F. Form: Exercise of Option

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.





8.64-1 Exercise of option

4. *Exercise of Option*.

4.1. *Conditions for Exercise of Option.* If Optionee is not in default under this Option Agreement and all conditions to the exercise of the option are satisfied or are waived in writing by Optionor, Optionee may exercise the option in accordance with this section and in no other manner. The option shall be exercised by delivering written notice from Optionee to Optionor before the expiration of the term of this option and in accordance with the notice provisions of _ _[*e.g., section 16*]_ _ (Exercise Notice). The Exercise Notice shall affirmatively state that the Optionee exercises the option without condition or qualification. Within _ _[*e.g., 3*]_ _ business days after exercise of the option, the parties shall execute and deliver the Purchase Agreement and shall deposit the funds and documents in escrow that the Purchase Agreement requires to be deposited when the Purchase Agreement is executed.

Comment: See §§8.20-8.24 for discussion of proper exercise of an option.

© The Regents of the University of California

§8.65 G. Form: Sequential Exercise of Option

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

8.65-1 Sequential exercise of option

[*If applicable, add the following option*]

[*Option: More than one parcel is subject to the option*]

4.2. *Sequential Exercise of Option.* The Property is described in Exhibit _ _[*e.g., A*]_ _ as _ _[*e.g., Parcel I, Parcel II, and Parcel III*]_ _. Optionee may exercise the option to purchase one or more of those parcels in accordance with the following provisions, and within the term and in the manner set forth in this Option Agreement.

Optionee may elect to purchase Parcel I, and the purchase price for Parcel I shall be _ _[*dollar amount*]_ _. _ _[*The option to purchase Parcel I must be exercised, if at all, on or before _ _[date]_ _.]_ _ If Optionee has elected to purchase Parcel I, Optionee may elect to purchase Parcel II, and the purchase price for Parcel II shall be _ _[*dollar amount*]_ _. _ _[*The option to purchase Parcel II must be exercised, if at all, on or before _ _[date]_ _.]_ _ If Optionee has elected to purchase Parcels I and II, Optionee may elect to purchase Parcel III, and the purchase price for Parcel III shall be _ _[*dollar amount*]_ _. _ _[*The option to purchase Parcel III must be exercised, if at all, on or before _ _[date]_ _.]_ _ On the exercise of any such option, the parties shall insert into the Purchase Agreement the description of the parcel for which the option is exercised, as that description is set forth in Exhibit _ _[*e.g., A*]_ _, and the purchase price for that parcel.

[*Continue*]

Comment: This clause anticipates that the developer may put the development together in stages and may decide not to pursue all stages. In such an agreement, the optionor must exercise care to ensure that, if the option is exercised for only a part of the property, the remaining parcels will be left with access and other factors important to satisfactory use by the optionor.

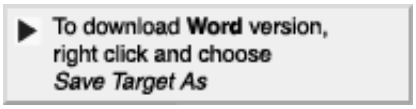
When a developer is trying to assemble a block of properties, it may condition the exercise and closing of the purchase on its ability to sign an option or purchase agreement for the balance of the properties. This may prove to be a delicate negotiation as it may not be in the developer's interest to let the property owners know that a block assemblage is intended.

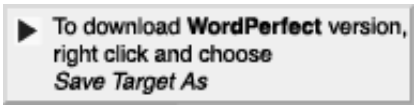
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/8 Options, Rights of First Refusal, Puts, and Similar Rights/§8.66 H. Form: Covenants and Warranties of Optionor Concerning Property

§8.66 H. Form: Covenants and Warranties of Optionor Concerning Property

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.





8.66-1 Covenants and warranties of optionor concerning property

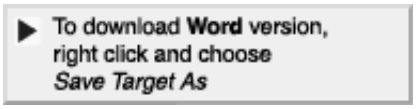
5. *Covenants and Warranties of Optionor Concerning Property.* Optionor covenants, warrants, and represents to Optionee that all the covenants, warranties, and representations set forth in section _ _ _ of the Purchase Agreement are true and correct.

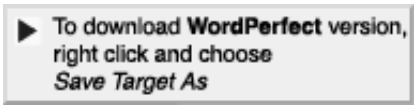
Comment: Typically, the optionor should give the same covenants and warranties on the property for the option term as are given for the purchase after the option is exercised, although in some instances there may be facts that can be warranted only after the option is exercised. On covenants and warranties generally, see §§4.101-4.120.

© The Regents of the University of California

§8.67 I. Form: Condition of Title

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.





8.67-1 Condition of title

6. *Condition of Title*.

6.1. *Preliminary Report.* Within _ _[*e.g., 10*]_ _ days after execution of this Option Agreement, Optionor shall deliver to Optionee a current preliminary report on the Property prepared by _ _[*specify*]_ _ Title Company, together with copies of all documents identified as exceptions in the report (collectively, Preliminary Report). Optionee shall have _ _[*e.g., 15*]_ _ days after receipt of the Preliminary Report in which to approve or disapprove any or all of the exceptions shown in the Preliminary Report.

6.2. *Approval of Exceptions in Preliminary Report.* Optionee shall disapprove exceptions shown in the Preliminary Report only by delivering written notice to Optionor within _ _[*e.g., 15*]_ _ days. If Optionee does not give written notice of disapproval within that time, Optionee shall be deemed to have approved all the exceptions shown in the Preliminary Report.

6.3. *Clearing of Exceptions in Preliminary Report.* If Optionee disapproves any exception to title, as provided above, Optionor shall notify Optionee within _ _[*e.g., 10*]_ _ days after receipt of such notice of disapproval if Optionor is unwilling to clear the disapproved exceptions. Optionor covenants that, if the option is exercised, Optionor shall, on or before closing under the Purchase Agreement, cause all disapproved exceptions to be removed as encumbrances against title to the Property except any exceptions that Optionor has notified Optionee that Optionor will not remove, in accordance with the notice provisions of this section.

6.4. *Failure to Clear Exceptions in Preliminary Report.* If Optionor notifies Optionee that Optionor will not remove one or more disapproved exceptions, Optionee may elect by delivering written notice to Optionor, within _ _[*e.g., 5*]_ _ days after receipt of Optionor's notice, to terminate this option and receive a refund of the option consideration paid to Optionor or to waive this condition, and this option shall then remain in full force and effect. Optionee's failure to give notice shall _ _[*waive this condition/terminate this option*]_ _.

Comment: The optionee has two principal reasons for wanting a preliminary report. The first is to investigate the state of record title and recover the option payment if title is not acceptable to the optionee. The second is to create a record of the encumbrances against title at the time of entering into the option, which can be referred to in the purchase and sale agreement with respect to both the covenant against further encumbrances and the condition addressing title to the property at closing.

An alternative, although less common, solution is for the optionee to obtain a preliminary report before entering into the option agreement and to set forth in the option agreement the condition of title the optionor agrees to convey at closing. On approval of condition of title generally, see §§4.50-4.70.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/8 Options, Rights of First Refusal, Puts, and Similar Rights/§8.68 J. Form: Investigation of Property

§8.68 J. Form: Investigation of Property

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

8.68-1 Investigation of property

7. *Investigation of Property*.

7.1. *Optionee's Right to Investigate Property.* At any time and from time to time during the term of the option, Optionee may enter the Property for purposes of inspection, survey, tests, design of improvements, and other actions reasonably related to the investigation by Optionee of the suitability of the Property for the Optionee's business purposes.

7.2. *Indemnification.* Optionee will indemnify, defend, and hold harmless Optionor from any loss, damage, claim, cost, lien, action, liability, or judgment (including, without limitation, Optionor's attorney fees and defense costs) (1) incurred for, from, or by any person or entity acting on behalf of, at the request of, or for the purpose of the actions of Optionee under this section; and (2) for personal injury, property damage, or other loss or damage of any kind arising from, resulting from, or in any way related to such entry.

7.3. *Changes to Property.* Optionee may make minor changes in the Property in the course of any investigation permitted under this Option Agreement (*e.g.,* soils borings), provided that the change or damage is only temporary, that it is reasonably necessary to the investigation of the physical characteristics of the Property, and that Optionee repairs such damage and restores the Property to its original condition promptly on completion of the investigation.

7.4. *Survival of Obligation.* The obligation under this section shall survive the termination of this Option Agreement or the expiration of the term of the option. On the termination of the Option Agreement for any reason or on expiration of the term of the option without exercise of the option, Optionee shall immediately restore the Property to its physical condition as of the date of this Option Agreement, at Optionee's sole cost.

7.5. *Insurance.* Optionee shall secure and maintain at all times during the term of this Option Agreement (1) a commercial general liability policy of insurance, including bodily injury and property damage coverage, written on an "occurrence" basis, with limits of not less than _ _[*e.g., $3,000,000*]_ _ insuring Optionee against injury to persons or damage to property arising from or in connection with any action permitted under this Option Agreement, naming Optionor as an additional insured under that coverage, and containing coverage for contractual liability for Optionee's obligations under this Option Agreement; and (2) workers' compensation and employers' liability insurance in accordance with California law. Optionee shall deliver to Optionor a copy of certificates evidencing such coverage in force, together with copies of the policies of insurance, before entering onto the Property. Each policy will contain a provision that such policy may not be terminated until _ _[*e.g., 30*]_ _ days after written notice of the proposed termination has been delivered to Optionor.

7.6. *Compliance With Law.* Optionee shall comply with all applicable governmental laws, ordinances, and regulations in the conduct of activity on the Property under this section. Before undertaking any activity on the Property that requires a governmental permit, Optionee will obtain the permit and pay any fee or expense required to obtain or carry out the permit.

Comment: This clause gives a broad right of inspection to the optionee. Such a broad right is most appropriate when there is no serious risk of liability to the owner or of damage to the property from the investigation activity, which is likely to be the case when, *e.g.,* the property is unimproved land. These expansive investigation rights should be carefully considered in light of the specific nature of the property involved and of the potential risk to the owner. See discussion in §8.7. (An owner should be particularly cautious in allowing environmental investigation that the owner

does not completely control. There are a number of risks to the owner from such an investigation (see chap 6), but of particular concern is the duty, required in many environmental statutes, to report environmental contamination once it is discovered.) See also §§4.77-4.82 on physical condition of the property.

© The Regents of the University of California

§8.69 K. Form: Governmental Permits

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

8.69-1 Governmental permits

8. *Governmental Permits*.

8.1. *Parties' Cooperation.* During the term of this Option Agreement, Optionee will seek certain governmental permits to develop the Property. Optionor shall cooperate with Optionee, shall take all actions and join in all applications, and shall execute all documents reasonably necessary to allow Optionee to pursue applications for and obtain such governmental permits, subject to the following terms and conditions:

8.2. *Indemnification.* Optionor shall not bear or become obligated to pay any expense or assume any liability in connection with any such governmental permit activity, and Optionee shall indemnify, defend, and hold harmless Optionor from any cost, loss, liability, or expense (including, without limitation, Optionor's attorney fees and defense costs) arising from or in connection with any such governmental permit activity.

8.3. *Burdens on Property.* Without Optionor's prior written consent, no governmental permit or approval that shall impose or increase any lien, encumbrance, tax, assessment, or other obligation (financial or otherwise) on the Property, or change the status of the Property in any manner that would increase the financial or other burdens or obligations of ownership of the Property or adversely affect the Optionor's ability to continue the current use of the Property, shall have any effect before closing under the Purchase Agreement. Optionor acknowledges that the processing by Optionee of applications to obtain governmental permits and investigation by Optionee with regard to the Property may directly or indirectly result in the discovery of toxic substances, endangered species, earthquake faults, title defects, or other matters that could affect the market value of the Property. If Optionee elects not to exercise its option to purchase, Optionor acknowledges that it may be required to undertake remedial actions on such defects. Optionee shall not be responsible for any loss in market value or any other damages Optionor incurs as a result of defects or conditions in the Property uncovered by any investigation of the Property conducted by Optionee or as a result of the applications for governmental permits.

8.4. *Disclosure of Applications*. Optionee shall submit to Optionor, at least _ _[*e.g., 5*]_ _ days before submission to the applicable governmental authority, copies of all applications and all studies, reports, and other documents that are part of such applications submitted for such governmental permits.

8.5. *Assignment of Applications and Permits.* All applications and governmental permits submitted or issued in the name of Optionee shall, to the maximum extent permitted by law, be assignable to Optionor and shall, in the event of expiration or earlier termination of the option, be assigned and transferred to Optionor. If Optionee does not exercise the option or complete the closing in accordance with the Purchase Agreement, Optionee shall assign to Optionor on request, and to the extent legally possible, all agreements between Optionee and its consultants and all reports procured by Optionee with regard to the Property.

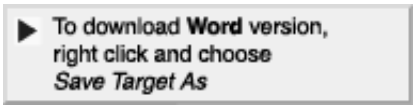
Comment: This provision assumes that the optionee will proceed with the governmental approval process, but the optionor will have significant control rights as protection against the effects that the process may have on the optionor's property. Like the investigation provisions of §8.68, this clause must be carefully considered and structured to address the specific issues that arise from the nature of the property and the governmental approval process, as well as from the rights that each party is willing to give the other and the obligations each party is willing to incur. If this issue is addressed in the option agreement, the clause is likely to be heavily negotiated and individually tailored to the specific transaction. On use and development of the property, see §§4.85-4.98.

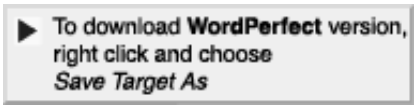
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/8 Options, Rights of First Refusal, Puts, and Similar Rights/§8.70 L. Form: Assignment of Option

§8.70 L. Form: Assignment of Option

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.





8.70-1 Assignment of option

[*Add one of the following alternatives*]

[*Alternative 1: Option may be assigned*]

9. *Option May Be Assigned.* Optionee may assign this option and the rights under it, but such assignment shall not relieve Optionee of any liability or obligation under this Option Agreement. An assignment shall be effective only if the assignee assumes all the duties and obligations of Optionee under this Option Agreement in a writing duly executed and delivered to Optionor.

[*Alternative 2: Option may not be assigned*]

9. *Option May Not Be Assigned*. This option is personal to Optionee. Optionee may not assign this option or any right under it. If any assignment is attempted, Optionee's rights under this option shall automatically terminate, without notice.

[*Continue*]

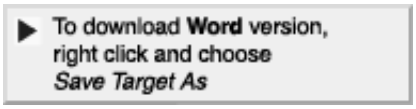
Comment: See also §§4.155-4.157 on assignment by buyer.

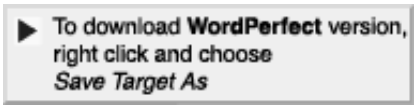
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/8 Options, Rights of First Refusal, Puts, and Similar Rights/§8.71 M. Form: Risk of Loss

§8.71 M. Form: Risk of Loss

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.





8.71-1 Risk of loss

10. *Risk of Loss.* If material loss or damage occurs to the Property during the option term but before exercise of the option, Optionee may elect to terminate this option by delivering written notice to Optionor within _ _[*e.g., 30*]_ _ days after discovering such loss or damage, and on such election Optionor shall immediately refund to Optionee the option consideration paid to Optionor (prorated on the basis of the number of days before termination compared with the number of days after termination until the end of the option term). Optionee shall have no other right or remedy in the event of such loss or damage.

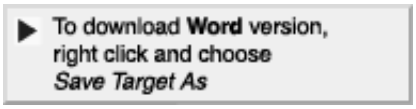
Comment: If loss or damage occurs after exercise of the option but before transfer of title or possession, the purchase and sale agreement should include provisions that will control the rights of the parties. This provision addresses the possibility of loss or damage before exercise of the option. In that case, the option consideration may be prorated, as suggested in this provision, or the risk of loss may be placed wholly on either the optionor (in which case the full option consideration is refunded if a loss occurs) or the optionee (in which case the optionor retains the full option consideration). If loss or damage occurs after exercise of the option, the purchase and sale agreement should include provisions controlling the parties' rights. On risk of loss, see §§4.137-4.139, 13.77-13.83.

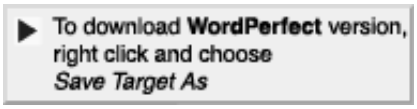
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/8 Options, Rights of First Refusal, Puts, and Similar Rights/§8.72 N. Form: Condemnation

§8.72 N. Form: Condemnation

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.





8.72-1 Condemnation

11. *Condemnation.* If at any time during the term but before exercise of the option either Optionor or Optionee receives notice of any condemnation or eminent domain proceeding, or any proceeding in lieu of condemnation, initiated against the Property, the party receiving notice shall promptly notify the other party of that fact. Optionee may elect to terminate this option by delivering written notice to Optionor within thirty days after Optionee receives such notice, and on such election Optionor shall immediately refund to Optionee the option consideration paid to Optionor (prorated on the basis of the number of days before termination compared with the number of days after termination to the end of the option term). Optionee shall have no other right or remedy in such condemnation or eminent domain action.

Comment: The issues of a provision addressing the parties' rights in a condemnation action arising either before or after exercise of the option are substantially identical to the risk-of-loss issues discussed in the comment in §8.71.

© The Regents of the University of California

§8.73 O. Form: Memorandum of Option to Be Recorded

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

8.73-1 Memorandum of option to be recorded

12. *Memorandum of Option to be Recorded.* On execution of this Option Agreement, Optionor and Optionee shall execute and record in the official records of the county in which the Property is located a memorandum of option in the form of the attached Exhibit _ _[*e.g., C*]_ _. Optionee shall pay the recording cost. Optionee covenants to execute and deliver to Optionor immediately on the expiration or earlier termination of the term of this Option Agreement a quitclaim deed in recordable form releasing and reconveying to Optionor all right, title, and interest of Optionee in the Property.

Comment: A recorded Memorandum of Option is vitally important to the optionee to protect against the priority of subsequent bona fide purchasers. See §8.22. For a form of Memorandum of Option, see §8.81.

Under CC §§884.010-884.030, the effect of the recorded Memorandum of Option expires 6 months after the option expires according to its terms or, if the memorandum does not specify the expiration date of the option, 6 months after the memorandum is recorded. On the issue of whether the recorded memorandum of option should describe any extension rights, see comment in §8.81. Even with that protection, the optionor wants the ability to require the optionee to deliver a quitclaim deed immediately on the option's expiration so that the property is not encumbered for any period before the statutory expiration date.

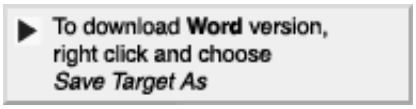
The optionee will usually not risk giving a quitclaim deed to the optionor to hold until the option terminates. If the optionor wants the security of an already executed quitclaim deed, it should be held in escrow by a title company or other acceptable escrow holder, with appropriate instructions.

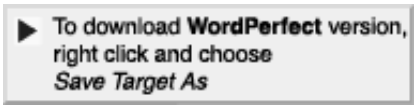
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/8 Options, Rights of First Refusal, Puts, and Similar Rights/§8.74 P. Form: Broker's Commission

§8.74 P. Form: Broker's Commission

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.





8.74-1 Broker's commission

13. *Broker's Commission.* The parties acknowledge that _ _[*Optionor/Optionee*]_ _ has used the services of _ _[*name*]_ _ (Broker) in obtaining this option. On execution and delivery of this Option Agreement, _ _[*Optionor/Optionee*]_ _ shall pay to Broker the sum of _ _[*dollar amount*]_ _ as a commission for the Broker's services in connection with this Option Agreement. Except as expressly set forth in this section or in the Purchase Agreement, neither party has dealt with any real estate agent or broker in connection with this Option Agreement in any manner that creates or may give rise to any right or claim for payment of a commission or other amount on account of this option. Each party shall indemnify, defend, and hold harmless the other from and against all loss, cost, and expense (including, without limitation, attorney fees and defense costs) incurred or suffered because of the breach of the foregoing representation and warranty arising from any claim for compensation founded on or as a result of acts asserted to have been performed on behalf of that party.

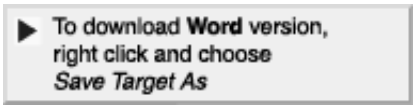
Comment: If a broker is involved in obtaining the option, he or she would not normally be entitled to a commission unless the option is exercised and the property is purchased. If a broker is entitled to a commission on execution of the option agreement regardless of whether the option is exercised, the option agreement should separately address the broker's commission rights for the option portion of the transaction. On broker's commission, see also §§2.91-2.121, 4.135.

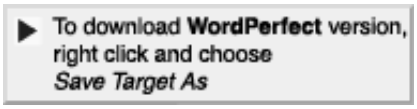
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/8 Options, Rights of First Refusal, Puts, and Similar Rights/§8.75 Q. Form: Time of Essence; Failure to Exercise

§8.75 Q. Form: Time of Essence; Failure to Exercise

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.





8.75-1 Time of essence; failure to exercise

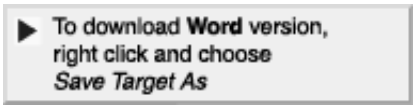
14. *Time of Essence; Failure to Exercise.* Time is of the essence of this Option Agreement and is a material term of this Option Agreement. If the option is not exercised as required by this Option Agreement before expiration of the term of the option that is set forth here, the option and all rights of Optionee shall automatically and immediately terminate without notice, and Optionee shall have no interest whatever in the Property. Once it has terminated, the option may not be revived by any subsequent payment or further action by Optionee.

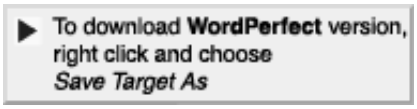
Comment: See also §4.152 on time-of-essence clauses.

© The Regents of the University of California

§8.76 R. Form: Attorney Fees

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.





8.76-1 Attorney fees

15. *Attorney Fees.* In the event of any action at law or in equity between the parties arising from or in connection with this Option Agreement, the prevailing party shall recover attorney fees and other costs incurred in that action in addition to any other relief, and such attorney fees and costs shall be included in and as a part of any judgment in such action.

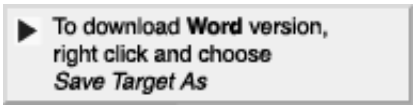
Comment: If the parties agree to an attorney fee clause, it should be included in the option contract as well as in the purchase and sale agreement so that it applies to all aspects of the transaction. See also §4.153 on attorney fees provisions.

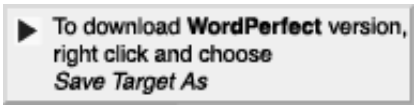
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/8 Options, Rights of First Refusal, Puts, and Similar Rights/§8.77 S. Form: Notices

§8.77 S. Form: Notices

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.





8.77-1 Notices

16. *Notices.* All notices and other communications authorized or required under this Option Agreement shall be in writing and shall be given by (1) personal delivery, (2) mailing by certified mail or registered mail, return receipt requested, postage prepaid, or United States express mail, or (3) delivery by commercially recognized courier service. Any such notice or other communication shall be deemed to have been given on the date of delivery or refusal to accept delivery if addressed as follows:

Optionor:	**Optionee:**
_ _[*Name*]_ _	_ _[*Name*]_ _
_ _[*Address*]_ _	_ _[*Address*]_ _

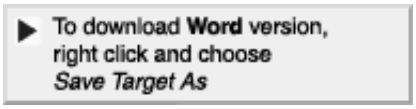
Comment: See also §4.151 on notices.

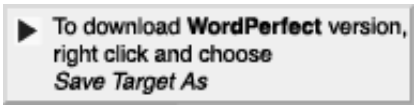
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/8 Options, Rights of First Refusal, Puts, and Similar Rights/§8.78 T. Form: Entire Agreement

§8.78 T. Form: Entire Agreement

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.





8.78-1 Entire agreement

17. *Entire Agreement.* This Agreement and all exhibits _ _[*, addenda, schedules, and agreements*]_ _ referred to in this Agreement constitute the complete, exclusive, and final statement of the terms of the agreement with respect to the option and may not be contradicted by evidence of any prior or contemporaneous agreement. This Option Agreement specifically supersedes any prior written or oral agreements between the parties. The language in all parts of this Option Agreement shall be construed as a whole in accordance with its fair meaning and without regard to California Civil Code §1654 or similar statutes. Neither party has been induced to enter into this Option Agreement by, and neither party is relying on, any representation or warranty outside those expressly set forth in this Option Agreement and the Purchase Agreement. No supplement, modification, or amendment of this Option Agreement shall be binding unless executed in writing by all parties.

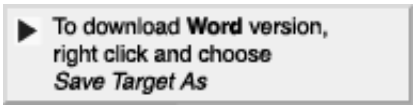
Comment: On purpose of entire agreement clause, see §4.159.

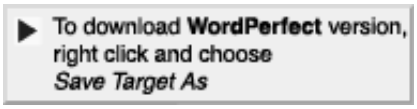
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/8 Options, Rights of First Refusal, Puts, and Similar Rights/§8.79 U. Form: Waiver

§8.79 U. Form: Waiver

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.





8.79-1 Waiver

18. *Waiver.* No waiver of any provision of this Option Agreement shall constitute or be deemed a waiver of any other provision, whether or not similar, nor shall any waiver constitute a continuing waiver. No waiver shall be binding unless it is executed in writing by the party making the waiver.

Comment: See also §4.154 on waivers.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/8 Options, Rights of First Refusal, Puts, and Similar Rights/§8.80 V. Form: Captions; Signatures

§8.80 V. Form: Captions; Signatures

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

8.80-1 Captions; signatures

19. *Captions.* The captions to the paragraphs of this Option Agreement are inserted for convenience only and shall not affect the intent of this Option Agreement.

IN WITNESS WHEREOF, the parties have executed this Option Agreement on the date set forth beside the signature of each.

Date: _ _ _ _ _ _ **Optionor:**

_ _[*Name of corporation*]_ _,
a _ _[*state of incorporation*]_ _ **corporation**

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

Date: _ _ _ _ _ _ **Optionee:**

_ _[*Name of corporation*]_ _,
a _ _[*state of incorporation*]_ _ **corporation**

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

Comment: Note that the "Date of the Option Agreement" used for reference purposes is set forth at the beginning of the agreement (see §8.59) and is not necessarily the date or dates set forth above opposite the signatures. See §4.12 for discussion of requirements for signature.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/8 Options, Rights of First Refusal, Puts, and Similar Rights/§8.81 W. Form: Memorandum of Option

§8.81 W. Form: Memorandum of Option

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

8.81-1 Memorandum of option

Recording requested by:)
After recording, return to:)
_____)

MEMORANDUM OF OPTION

This Memorandum of Option is made on _ _[*date*]_ _, between _ _[*name*]_ _ (Optionor) and _ _[*name*]_ _ (Optionee), who agree as follows:

1. Optionor grants to Optionee the option to purchase the real property described _ _[*in Exhibit _ _ _/as follows:*]_ _ (Option Property).

2. The term of the option is for a period of _ _[*e.g., 1 year*]_ _ beginning on _ _[*date*]_ _, and terminating on _ _[*date*]_ _. _ _[*Describe any extension options*.]_ _

3. The option that is the subject of this Memorandum of Option is granted in accordance with an option agreement between optionor and optionee concerning the option property and dated _ _[*date*]_ _ (Option Agreement). This Memorandum of Option is prepared for the purpose of recordation and shall not alter or affect in any way the rights and obligations of optionor and optionee under the Option Agreement. In the event of any inconsistency between this Memorandum of Option and the Option Agreement, the terms of the Option Agreement shall control.

IN WITNESS WHEREOF, the parties have executed this Option Agreement.

Date: _ _ _ _ _ _ **Optionor:**

_ _[*Name of corporation*]_ _,
a _ _[*state of incorporation*]_ _ **corporation**

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

[*Acknowledgment*]

Date: _ _ _ _ _ _ **Optionee:**

_ _[*Name of corporation*]_ _,
a _ _[*state of incorporation*]_ _ **corporation**

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

[*Acknowledgment*]

Comment: For discussion of a Memorandum of Option, see §§8.22, 8.73. The form includes a statement of when the

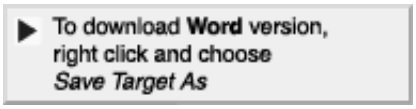
option terminates because of the effect of CC §§884.010-884.030, as discussed in §8.73. If the optionee has the right to extend the option for multiple terms, the optionor probably will not want the recorded Memorandum of Option to describe the extensions. The optionee can ensure that a recorded Memorandum of Option will remain in effect in such circumstances by requiring the optionor to deposit with a title company, at the time the Option Agreement is executed, a Memorandum of Option for each extension period with appropriate instructions to permit the title company to record it automatically if the option term extension becomes effective.

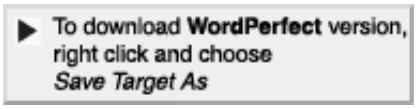
The recorded Memorandum of Option must be executed and acknowledged by all parties identified as optionors in the Memorandum of Option. Govt C §27288.

© The Regents of the University of California

§8.82 X. Form: Right of First Offer Agreement

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.





8.82-1 Right of first offer agreement

_.1. This Right of First Offer Agreement (Agreement) is made between _ _[*name*]_ _ (Optionor) and _ _[*name*]_ _ (Optionee). This Agreement is dated _ _[*date*]_ _, for reference purposes only.

_.2. Right of First Offer. Subject to the terms and conditions specified in this Agreement, in the event the Optionor proposes to offer or sell the Property described in more detail on Exhibit _ _[*e.g., A*]_ _ attached hereto (Property), the Offeror shall first offer to sell the Property to Offeree in accordance with the following provisions of this Agreement:

_.2.1. Offeror shall deliver a notice (Offer Notice) to Offeree stating (i) its good faith intention to sell the Property, and (ii) the price, terms, and conditions on which it proposes to sell the Property.

_.2.2. By written notification given by Offeree (Acceptance Notice), within _ _[*e.g., 30*]_ _ calendar days after the giving of the Offer Notice, Offeree may elect to purchase the Property on the terms and conditions specified in the Offer Notice.

_.2.3. If the Acceptance Notice is not given, or not given in a timely manner, then Offeror may, during the _ _[*e.g., 90*]_ _-day period (Permitted Sale Period) following the expiration of the period provided in section _ _[*e.g., _.2.2*]_ _ above, offer to sell the Property to any person or persons at a price not less than, and on terms and conditions no more favorable than, those specified in the Offer Notice. If Offeror does not complete the sale of the Property before the end of the Permitted Sale Period, the right of first offer provided hereunder shall be deemed to be revived and the Property shall not be offered for sale or sold unless first reoffered to Offeree in accordance with this section.

_.2.4. The right of first offer in this section shall not be applicable to sales or transfers of the Property on account of: _ _[*e.g., intrafamily transfers*]_ _.

_.2.5. The right of first offer set forth in this section may not be assigned or transferred by Offeree except to _ _[*name*]_ _.

_.2.6. This Right of First Offer shall terminate on _ _[*date*]_ _.

Comment: See §8.58 for a discussion of the right of first offer. Additional sections should be added to complete the terms and conditions applicable to the agreement. Consider including forms set forth in §§8.73-8.80.

Exceptions to the right of first offer may be required for transactions such as intrafamily transfers, transfers when there is no change of control of the offeror or its successor, transfers by operation of law, and involuntary transfers. Consideration should be given for automatic extensions of the time limit to close the sale of the property when the sale is delayed through circumstances beyond the reasonable control of offeror.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/8 Options, Rights of First Refusal, Puts, and Similar Rights/§8.83 Y. Form: Right of First Refusal Agreement

§8.83 Y. Form: Right of First Refusal Agreement

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§8.59-8.83.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

8.83-1 Right of first refusal agreement

_.1. This Right of First Refusal Agreement (Agreement) is made between _ _[*name*]_ _ (Offeror) and _ _[*name*]_ _ (Offeree). This Agreement is dated _ _[*date*]_ _, for reference purposes only.

_.2. Right of First Refusal. Offeror shall not sell the property described on Exhibit _ _[*e.g., A*]_ _ attached hereto (Property) except in accordance with the provisions of this Agreement. Any such sale shall be pursuant to a written offer (Offer) from Qualified Purchaser, defined below, setting forth the terms and conditions for such proposed purchase, provided that such terms and conditions must provide for an all-cash purchase price and a closing date of not less than _ _[*e.g., 30*]_ _ days after acceptance of the Offer. A Qualified Purchaser shall be an independent third party that is not directly or indirectly owned or controlled by or under common control with Offeree and that intends to purchase the Property for its own account.

_.2.1. If Offeror receives an Offer that Offeror is willing to accept, Offeror shall give Offeree a copy of the Offer and certify to Offeree that the proposed purchaser is a Qualified Purchaser (Offer Notice).

_.2.2. Offeree shall have _ _[*e.g., 30*]_ _ days from the delivery of the Offer Notice (Acceptance Period) within which to notify the Offeror of its election to purchase the Property under the terms and conditions specified in the Offer, by giving written notice to the Offeror (Acceptance Notice) of such election.

_.2.3. On delivery of the Acceptance Notice, the Offeror and Offeree shall forthwith proceed to consummate the sale and purchase of the Property on the terms and conditions set forth in the Offer.

_.2.4. If the Acceptance Notice is not given in a timely manner, then the Offeror may thereafter proceed to sell the Property any time within _ _[*e.g., 90*]_ _ days after the expiration of the Acceptance Period, on the terms and conditions set forth in the Offer, free and clear of any rights of Offeree under this Right of First Refusal with respect to that sale only.

_.2.5. Any sale or proposed sale on any other terms and conditions or after expiration of said _ _[*e.g., 90*]_ _ days shall be a new sale subject to all of the terms of this Right of First Refusal.

_.2.6. The right of first refusal set forth in this section shall not be applicable to sales or transfers of the Property on account of: _ _[*e.g., intrafamily transfers*]_ _.

_.2.7. The right of first refusal set forth in this section may not be assigned or transferred by Offeree except to _ _[*name*]_ _.

_.2.8. This Right of First Refusal shall terminate on _ _[*date*]_ _.

Comment: See §8.58 for a discussion of the right of first refusal. Because an adequate property description is an essential element of an option contract (see §8.9), it is good practice to make a legally sufficient description a part of the option contract. Additional sections should be added to complete the terms and conditions applicable to the agreement. Consider including forms set forth in §§8.73-8.80.

Exceptions to the right of first refusal may be required for transactions such as intrafamily transfers, transfers when there is no change of control of the offeror or its successor, transfers by operation of law, and involuntary transfers. Consideration should be given for automatic extensions of the time limit to close the sale of the property when the sale is delayed through circumstances beyond the reasonable control of offeror.

this Agreement, except to the extent Buyer has received a credit therefor against the Purchase Price under this Agreement.

_.8.2. Buyer agrees to defend, indemnify, and hold harmless Seller from and against any and all loss, damage, cost, claim, liability, or expense (including court costs and reasonable attorney fees) suffered or incurred by Seller arising out of any events relating to the period following the Cutoff Time, excluding any loss, damage, cost, claim liability, or expense (including court costs and reasonable attorney fees) resulting from the gross negligence or willful misconduct of Seller, or any liability or obligation assumed by Buyer under this Agreement or in any agreement executed and/or delivered at the Closing, or resulting from Buyer's failure to pay any item for which it received a credit against the Purchase Price under this Agreement.

Comment: Sales tax will be payable on the sale of the hotel's tangible personal property, because the seller will hold a resale certificate and there will probably be no exemption from the requirement to pay sales tax. This form provides that the seller will pay the sales taxes. Other agreements provide for an equal division of the sales taxes between the seller and the buyer. See Sales and Mergers of California Businesses §§3.42-3.44 (Cal CEB 2002).

© The Regents of the University of California

9

Seller Financing

Alice L. Akawie
Lauren M. LaPietra
W. Stephen Wilson

I. INTRODUCTION
- A. Why Seller Financing? §9.1
- B. Lawyer's Role
  - 1. Financing §9.2
  - 2. Structuring the Buyer §9.3
  - 3. Standard of Care
    - a. To Clients §9.4
    - b. To Third Parties §9.5
- C. Usury Considerations
  - 1. Seller Financing §9.6
  - 2. Third Party Wraparound Financing §9.7
- D. Antideficiency Laws
  - 1. Applicability of Antideficiency Protections §9.8
  - 2. Exceptions to Antideficiency Protections §9.9

II. DISCLOSURE REQUIREMENTS
- A. Seller's Disclosures
  - 1. Arranger of Credit §9.10
  - 2. Balloon Payment §9.11
  - 3. Appraisals §9.12
- B. Form: Seller Financing Addendum and Disclosure (CAR Form SFA) §9.13

III. SELLER-FINANCING DEVICES
- A. Installment Land Contract §9.14
  - 1. Distinguished From Purchase and Sale Agreement §9.15
  - 2. Decline in Popularity; Disadvantages §9.16
  - 3. Protective Statutory and Regulatory Provisions §9.17
- B. Lease With Option to Purchase
  - 1. Reasons to Use §9.18
  - 2. Hidden Security Device §9.19
  - 3. Distinguishing Lease-Option From Hidden Security Device
    - a. How Courts Distinguish §9.20
    - b. How Tax Treatment Differs §9.21
- C. Promissory Note Secured by Mortgage or Deed of Trust §9.22
- D. Buyer's Obligation to Comply With FIRPTA §9.23

IV. POSTPONING SELLER'S INCOME TAX LIABILITY
- A. Installment Method of Reporting Gain §9.24
  - 1. Statutory Requirements; Definitions §9.25
  - 2. Computation Examples
    - a. Typical Installment Sale §9.26
    - b. Effect of Recapture §9.27
    - c. Mortgage in Excess of Basis §9.28
  - 3. Wraparound Financing §9.29
  - 4. Seller's Ability to Limit Prepayments
    - a. Restrictions on Limitations on Prepayment §9.30
    - b. Monetary Penalty on Prepayments §9.31
  - 5. Treatment of Dealers §9.32
  - 6. Disposition of Installment Obligations §9.33
  - 7. Original Issue Discount and Imputed Interest §9.34
    - a. Original Issue Discount §9.35

b. Imputed Interest Rules §9.36
c. Applicable Federal Rate §9.37
B. Open-Ended or Contingent Sales Price §9.38
C. Relationship to Buyer's Financing Needs §9.39

V. DEFERRING PAYMENTS; FORM PROVISIONS FOR PURCHASE AND SALE AGREEMENT
A. Form: Cash Downpayment §9.40
B. Form: Credit for Existing Encumbrances §9.41
C. Promissory Note for Balance Due
1. Form of Loan Documents §9.42
2. Security; Title Insurance §9.43
3. Computation of Payments §9.44
4. Form: Note for Balance; First-Year Payments Limited §9.45
5. Form: Note for Balance; Annual Payments Limited §9.46
D. Form: Acceleration on Default §9.47

VI. RETAINING EXISTING ENCUMBRANCES
A. Buyer's Assumption of, or Sale Subject to, Existing Encumbrances §9.48
1. Due-on-Sale and Due-on-Encumbrance Clauses §9.49
a. Enforceability of Clauses
(1) Due-on-Sale Clauses §9.50
(2) Due-on-Encumbrance Clauses §9.51
b. Prohibition on Prepayment Penalties §9.52
c. Impact on Buyer §9.53
2. Transferability of Government Financing §9.54
3. Impact of Antideficiency Laws §9.55
4. Restrictions on Foreclosure §9.55A
B. All-Inclusive Note and Deed of Trust
1. Definition §9.56
2. Purposes and Uses
a. Higher Effective Interest Rate §9.57
b. Reporting Interest for Tax Purposes §9.58
c. Seller's Control Over Security §9.59
d. Tax Considerations; Installment Reporting §9.60
3. Drafting All-Inclusive Instruments §9.61
a. Consistency With Underlying Obligations and Encumbrances; Prepayments; Amortization §9.62
b. Rights in Case of Default §9.63
c. Foreclosure §9.64
4. Form: Provision in Purchase and Sale Agreement for All-Inclusive Financing §9.65

VII. SELLER'S PARTICIPATION IN BUYER'S FINANCING
A. Subordination §9.66
1. Subordinating to Construction Loans
a. Competing Factors §9.67
b. Methods of Providing First Lien §9.68
(1) Order of Recordation §9.69
(2) Automatic Subordination; Subordination Agreement §9.70
c. Risks to Seller §9.71
d. Seller's Benefits §9.72
2. Types of Subordination Agreements §9.73
a. Executory Subordination Agreement §9.74
(1) Enforceable: Certain and Reasonable §9.75
(2) Required Terms §9.76
(3) Form: Optional Terms §9.77
(4) Form: Executory Subordination Provision in Purchase Agreement §9.78
(5) Subordination Addendum
(a) Information to Include in Subordination Addendum §9.79
(b) Form: Subordination Addendum §9.80
(c) Form: Subordination to Permanent Loan §9.81
(d) Form: Execution of Additional Subordination Agreement §9.82
b. Executed Subordination Agreement §9.83
(1) Discrepancy Between Agreement and Loan §9.84
(2) Misapplication of Funds §9.85
(3) Automatic Subordination Agreement §9.86
(4) Form: Automatic Subordination Agreement §9.87

c. De Facto Subordination Agreement §9.88
3. Cautionary Language Required §9.89
a. Automatic Subordination §9.90
b. Security Instrument Permits Proceeds to be Used for Nonimprovement Purposes §9.91
c. Agreement Causes Security Interest to Become Junior §9.92
d. Agreement Permits Proceeds to be Used for Nonimprovement Purposes §9.93
e. Right to Waive §9.94
4. Effect of Subordination on Antideficiency Rules
a. Exemption From Antideficiency Protection §9.95
b. Express Waiver Not Required §9.96
c. Mere Promise to Subordinate Not Sufficient §9.97
d. Nonconstruction Loan §9.98
e. Relevance of Loan Amount §9.99
B. Release and Partial Reconveyance §9.100
1. Requirement of Certainty and Fairness
a. Impact on Specific Performance §9.101
b. Impact on Damages §9.102
2. Subdivision Requirements
a. Subdivision Map Act §9.103
b. Subdivided Lands Act §9.104
3. Form: Partial Release of Determined Lots §9.105
4. Form: Partial Release (Lots Not Determined); Limiting Buyer's Discretion §9.106
5. Form: Partial Release (Lots Not Determined); Adjustment of Release Price §9.107
6. Form: Unencumbered Conveyance at Close of Escrow §9.108
7. Form: Substituted Security for Releases §9.109
8. Form: Release on Condemnation Award §9.110

© The Regents of the University of California

I. INTRODUCTION

§9.1 A. Why Seller Financing?

Few buyers of real property pay the purchase price entirely from their own funds. Most finance the purchase by borrowing from an institutional, governmental, or individual lender; by acquiring the property subject to existing encumbrances; by having the seller defer payment of at least a portion of the price; or by a combination of these devices. The indebtedness resulting from financing is usually secured by withholding title to the property until payment has been made, by encumbering title to the property, or by encumbering some other property. In addition, the seller has a "vendor's lien" on the property for as much of the price as remains unpaid, to the extent that the property is otherwise unsecured. CC §3046.

Although most funds for real property financing come from institutional lenders, such as savings and loan associations and banks, seller financing often plays an important role. Both parties to a sale may wish to defer payment of all or part of the purchase price. The seller may want the tax advantages of installment reporting (see §9.24) or may want to negotiate a higher purchase price in exchange for deferring payment. For the buyer, seller financing generally provides the protections of antideficiency legislation and the avoidance of various lender costs such as points and appraisal fees (CCP §580b; but see *Spangler v Memel* (1972) 7 C3d 603, 102 CR 807, discussed in §§9.71-9.72, 9.95). Frequently, sellers are willing to give more favorable loan terms and to lend a greater amount of the purchase price than are outside lenders.

If the seller defers part of the price and encumbers the property, the seller may also be asked to participate in the buyer's financing by subordinating the priority of the lien to liens for financing obtained by the buyer from third parties or by agreeing to release the lien from portions of the property as the property is developed or sold. On subordination, see §§9.66-9.99. On release, see §§9.100-9.110.

© The Regents of the University of California

B. Lawyer's Role

§9.2 1. Financing

The lawyer's role in the financing aspects of the transaction may be crucial. He or she may be called on to perform a wide range of functions, beginning with negotiating the purchase price and the extent to which the seller will participate in financing the buyer's development of the property. Counsel, either alone or together with the seller's accountant, may be required to structure the financing to minimize adverse tax consequences to the seller or to satisfy the requirements of title insurance companies and lenders. The lawyer must either draft the purchase and sale agreement or evaluate one that someone else has drawn. If the buyer needs time to arrange third party financing, the lawyer must make sure that the agreement allows the necessary time. The seller's lawyer must make certain that the buyer is not allowed to postpone the sale unreasonably and that, if the delay is to be substantial, the seller will be protected against possible fluctuations in value and lost opportunities.

If the seller is to provide financing, the type of financing and the security arrangement must be considered carefully because they may have significantly different tax consequences and different remedies available in the event of breach or default.

© The Regents of the University of California

§9.3 2. Structuring the Buyer

The buyer's attorney must determine the most appropriate legal structure for the buyer. Would title to the property best be taken in the name of the individuals involved, or in a partnership, corporation, or limited liability company? There are serious issues of liability, control, management, and tax implications that the buyer must consider. For a discussion of issues to consider in taking title, see §§4.22-4.28.

It is increasingly common for buyers to take title to property in the form of a single purpose entity (SPE) that is formed solely to hold title to the property and to conduct no other business. Moreover, the lender may require that the SPE be structured as a bankruptcy-remote entity, separate from any other entities owned by the individuals forming the SPE. In this manner, the SPE would be unaffected by a bankruptcy of any related entities. For a discussion of single-purpose entities, see California Real Estate Finance Practice: Strategies and Forms §§1.96, 10.14-10.17 (Cal CEB 2000). The formation of such entities is a complex process and should be handled with care.

Finally, the lawyer for the buyer will have an additional important task. He or she will often be required to issue a legal opinion to the lender regarding the formation of the buyer; and, if a bankruptcy-remote entity was formed, to issue a nonconsolidation opinion (*i.e.*, an opinion that the SPE will not be consolidated with any related entities if there should be a bankruptcy of any of the related entities). See §§1.121-1.130 for a discussion of legal opinions.

© The Regents of the University of California

3. Standard of Care

§9.4 a. To Clients

The need for the attorney to demonstrate a high degree of care, skill, and diligence in advising clients and drafting documents relating to real property financing cannot be overemphasized. Different financing methods present different drafting problems and possibly different enforcement problems.

EXAMPLE: A purchase agreement with an improperly drafted subordination or partial release clause may be unenforceable or may subject the sale to rescission. See §§9.75, 9.101-9.102. It may also subject the drafting attorney to liability.

Of particular interest is *Starr v Mooslin* (1971) 14 CA3d 988, 92 CR 583, which involved a transaction in which the seller agreed to take back a promissory note for the balance of the purchase price and to subordinate her lien to a construction loan. The seller recovered a substantial damage award against her attorney for his negligence in drafting escrow instructions that failed to provide adequate protection against the possibility of the buyer's default on the construction loan, despite the attorney's reliance on custom and practice of local escrow holders. See also §1.14 on the attorney's duty of care.

© The Regents of the University of California

§9.5 b. To Third Parties

An attorney's duty to the client in a real property sales transaction generally does not extend to third parties involved in the transaction. See *St. Paul Title Co. v Meier* (1986) 181 CA3d 948, 226 CR 538, in which an escrow agent, sued by a buyer for failure to properly implement escrow instructions, cross-complained against the buyer's attorney on the theory that the attorney created confusing escrow instructions. The court of appeal affirmed a summary judgment in favor of the attorney, holding that he owed no professional duty to an escrow agent whom he did not represent. The attorney may be liable to the third party, however, if the third party is a third party beneficiary of the transaction or there is foreseeable harm to the third party as a result of professional negligence. See *Shawmut Bank, N.A. v Kress Assoc.* (9th Cir 1994) 33 F3d 1477, 1505, in which a trustee of bonds was permitted to go to trial on a claim against a law firm hired by the bond issuer to draft the bond indenture. In denying a summary judgment against the trustee, the Ninth Circuit held that the trustee may have been a third party beneficiary of the law firm's drafting, who as such would be entitled to sue for negligent preparation of the trust documents.

© The Regents of the University of California

C. Usury Considerations

§9.6 1. Seller Financing

There are several exceptions to usury that could protect a lender involved in real estate purchase financing. First, if the seller either provides a note secured by a deed of trust or takes back an all-inclusive note and wraparound deed of trust, the transaction should be exempt from the usury law under the time-price differential doctrine, which distinguishes a credit sale of property from a loan or forbearance, freeing the credit sale from the restrictions of Cal Const art XV, §1. *Ghirardo v Antonioli* (1994) 8 C4th 791, 35 CR2d 418; *Southwest Concrete Prods. v Gosh Constr. Corp.* (1990) 51 C3d 701, 274 CR 404; *Boerner v Colwell Co.* (1978) 21 C3d 37, 145 CR 380; *Verbeck v Clymer* (1927) 202 C 557, 261 P 1017. See Brown, *The Current Status of the Time-Price Differential Doctrine in California*, 2 CEB Real Prop L Rep 93, 109 (Aug., Oct. 1979). For a further discussion of seller financing, see California Mortgage and Deed of Trust Practice §9.130 (3d ed Cal CEB 2000). Second, if the loan is structured with the good faith participation of a licensed real estate broker, it is exempt from usury under Cal Const art XV, §1. See §2.9.

If the lender is able to demonstrate that its loan transaction comes within a specific constitutional or statutory exception to the usury law, the lender's actual intent is irrelevant. The transaction is excluded from usury even if the lender's intent is to violate the spirit of the usury law. *Jones v Wells Fargo Bank* (2003) 112 CA4th 1527, 5 CR3d 835. See California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 3 (4th ed Cal CEB 2009) for other usury exemptions.

© The Regents of the University of California

§9.7 2. Third Party Wraparound Financing

If a third party provides wraparound financing, usury may be a problem. If the borrower remains personally liable on the underlying indebtedness, then the new lender (the payee on the wraparound note) has lent only the amount of the payee's equity in the note, not its full face amount, and only this equity would be used in deciding whether the interest rate is usurious. However, if the payee of the wraparound note becomes personally liable for the underlying debt, it can be argued that the full principal amount of the wrapped indebtedness, not just the payee's equity in the wrap, should be used to calculate the true interest rate for usury purposes. The suggested rationale is that the payee is then lending credit to the buyer and should be entitled to interest on the full amount of the credit extended, not just the equity. See 4 Miller & Starr, California Real Estate §§10:22-10:23 (3d ed 2000); Comment, *The Wrap-Around Mortgage: A Critical Inquiry,* 21 UCLA L Rev 1529 (1974); Comment, *The Wrap-Around Deed of Trust: An Answer to the Allegations of Usury,* 10 Pac LJ 923 (1979). See also California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 9 (4th ed Cal CEB 2009).

NOTE: Any lender who is considering taking advantage of the wraparound loan should take into account CC §2923.5, which imposes limitations on the lender's right to conduct a nonjudicial foreclosure sale in connection with owner-occupied real property if the underlying loan was made between January 1, 2003, and December 31, 2007. If a lender proposes to wrap around an underlying loan that is subject to these limitations, it is likely that the same limitations will apply to the wraparound loan.

© The Regents of the University of California

D. Antideficiency Laws

§9.8 1. Applicability of Antideficiency Protections

Under CCP §580b, no deficiency judgment is available after the foreclosure of seller financing, regardless of the size of the property or the amount borrowed. The protection of §580b extends not only to the borrower but also to any party who is the legal equivalent of the borrower, such as the settlor-trustee of an inter vivos trust in which the trust is the borrower under a loan. See *Cadle Co. II v Harvey* (2000) 83 CA4th 927, 100 CR2d 150.

Protection against deficiency judgments afforded to purchase money borrowers by §580b may not be waived either at the time of or after sale of the property (*DeBerard Props. v Lim* (1999) 20 C4th 659, 85 CR2d 292) nor may antideficiency protection be waived indirectly. *Lawler v Jacobs* (2000) 83 CA4th 723, 100 CR2d 52 (CCP §580b precluded seller-lender's fraud claim against purchase money borrowers based on borrowers' written promise to remain liable for deficiency following foreclosure). Moreover, the protection of §580b applies only to the monetary obligations created as consideration for the purchase of the real property interest; it does not apply to liability for "waste" on the property (*Nippon Credit Bank v 1333 N. Cal. Blvd.* (2001) 86 CA4th 486, 103 CR2d 421) or any other tort obligations that might have arisen in connection with the transaction. See *Kolodge v Boyd* (2001) 88 CA4th 349, 105 CR2d 749. See also discussion of *Lawler* in Comment, 23 CEB Real Prop L Rep 313 (Nov. 2000).

© The Regents of the University of California

§9.9 2. Exceptions to Antideficiency Protections

A sizable body of case law has created an exception to the rule discussed in §9.8 for a seller whose financing was subordinated to a new loan secured by a first deed of trust on the property. This exception to CCP §580b has almost always been limited to situations in which the seller subordinates to a significant construction loan. Moreover, such protections will apply to protect the borrower even when a note is given as security for the purchase of both personal and real property (mixed collateral). *Sherwood-Trimble Med. Group v 1001 Venice Blvd. Partnership* (1999) 75 CA4th 872, 89 CR2d 533.

NOTE: The exception will not apply if the lender agrees merely to subordinate to future construction, but fails in fact to subordinate. *Crookall v Davis, Punelli, Keathley & Willard* (1998) 65 CA4th 1048, 77 CR2d 250. See §§9.95-9.97.

Generally, the protections of CCP §580b do not apply when the seller secures its purchase price with a lien on property other than that being sold (*Kurtz v Calvo* (1999) 75 CA4th 191, 89 CR2d 99), unless the court determines that the property being sold and the property being encumbered were both transferred as a "package" that happened to close at different times (*Conley v Matthes* (1997) 56 CA4th 1453, 66 CR2d 518). See discussion in Bernhardt, *Death Knell for the "Other Security" Deficiency Exception? Coney v Matthes*, 20 CEB Real Prop L Rep 260 (Nov. 1997).

For further discussion of antideficiency laws, see California Mortgages, Deeds of Trust, and Foreclosure Litigation chap 5 (4th ed Cal CEB 2009).

© The Regents of the University of California

II. DISCLOSURE REQUIREMENTS

A. Seller's Disclosures

§9.10 1. Arranger of Credit

Under CC §§2956-2967, when a one-to-four-unit dwelling is involved, specified written disclosures must be made to both the buyer and the seller if financing is provided by an arranger of credit. An "arranger of credit" is broadly defined in CC §2957(a) as any party to the transaction who is a real estate licensee or attorney if neither party is represented by a licensed real estate agent, or any nonparty who is involved in developing or negotiating credit terms, who participates in completion of credit documents, or who directly or indirectly receives compensation for arranging the financing or from the transaction that the financing facilitates. Exceptions to the definition of "arranger of credit" are the escrow agent and any attorney who represents one of the parties. A violation of §§2956-2967 does not invalidate the credit or security document, but it creates a cause of action for actual damages incurred by the seller or the buyer as a result of the violation. CC §2965.

© The Regents of the University of California

§9.11 2. Balloon Payment

To the extent that seller financing under CC §§2956-2967 involves a balloon payment on the note, CC §2966 requires the seller to give at least 90 and no more than 150 days' prior notice of the upcoming payment, including the amount due and any refinancing rights that may exist. For further discussion of CC §§2956-2967, see Fishkin, *Disclosures in Creative Financing: Disclosures I, II, and III*, 6 CEB Real Prop L Rep 133 (Oct. 1983). See also §6.69.

© The Regents of the University of California

§9.12 3. Appraisals

Business and Professions Code §11423(b) requires that borrowers be notified of their right to receive a copy of any appraisal report for which they have paid. Business and Professions Code §11423(g) seems to create an exception from the notification requirement when the lender obtains an appraisal on property owned by the lender, whether or not the borrower paid for the appraisal. Thus, sellers may not need to comply with this requirement. Federal law provides a similar right to obtain a copy of the appraisal. 12 CFR §202.14.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.13 B. Form: Seller Financing Addendum and Disclosure (CAR Form SFA)

§9.13 B. Form: Seller Financing Addendum and Disclosure (CAR Form SFA)



CALIFORNIA ASSOCIATION OF REALTORS®

SELLER FINANCING ADDENDUM AND DISCLOSURE

(California Civil Code §§2956-2967)

(C.A.R. Form SFA, Revised 10/02)

This is an addendum to the ☐ Residential Purchase Agreement, ☐ Counter Offer, or ☐ Other _____ _____, ("Agreement"), dated _____,
On property known as _____ ("Property"),
between _____ ("Buyer"),
and _____ ("Seller").
Seller agrees to extend credit to Buyer as follows:

1. **PRINCIPAL; INTEREST; PAYMENT; MATURITY TERMS:** ☐ Principal amount $ _____, interest at _____% per annum, payable at approximately $ _____ per ☐ month, ☐ year, or ☐ other _____, remaining principal balance due in _____ years.
2. **LOAN APPLICATION; CREDIT REPORT:** Within **5 (or** ☐ _____**)** **Days** After Acceptance: **(a)** Buyer shall provide Seller a completed loan application on a form acceptable to Seller (such as a FNMA/FHLMC Uniform Residential Loan Application for residential one to four unit properties); and **(b)** Buyer authorizes Seller and/or Agent to obtain, at Buyer's expense, a copy of Buyer's credit report. Buyer shall provide any supporting documentation reasonably requested by Seller. Seller may cancel this Agreement in writing if Buyer fails to provide such documents within that time, or if Seller disapproves any above item within **5 (or** ☐ _____**)** **Days** After receipt of each item.
3. **CREDIT DOCUMENTS:** This extension of credit by Seller will be evidenced by: ☐ Note and deed of trust; ☐ All-inclusive note and deed of trust; ☐ Installment land sale contract; ☐ Lease/option (when parties intend transfer of equitable title); OR ☐ Other (specify) _____

THE FOLLOWING TERMS APPLY ONLY IF CHECKED. SELLER IS ADVISED TO READ ALL TERMS, EVEN THOSE NOT CHECKED, TO UNDERSTAND WHAT IS OR IS NOT INCLUDED, AND, IF NOT INCLUDED, THE CONSEQUENCES THEREOF.

4. ☐ **LATE CHARGE:** If any payment is not made within ____ **Days** After it is due, a late charge of either $ _____, or ____% of the installment due, may be charged to Buyer. **NOTE:** On single family residences that Buyer intends to occupy, California Civil Code §2954.4(a) limits the late charge to no more than 6% of the total monthly payment due and requires a grace period of no less than 10 days.
5. ☐ **BALLOON PAYMENT:** The extension of credit will provide for a balloon payment, in the amount of $ _____, plus any accrued interest, which is due on _____ (date).
6. ☐ **PREPAYMENT:** If all or part of this extension of credit is paid early, Seller may charge a prepayment penalty as follows (if applicable): _____. Caution: California Civil Code §2954.9 contains limitations on prepayment penalties for residential one-to-four unit properties.
7. ☐ **DUE ON SALE:** If any interest in the Property is sold or otherwise transferred, Seller has the option to require immediate payment of the entire unpaid principal balance, plus any accrued interest.
8.* ☐ **REQUEST FOR COPY OF NOTICE OF DEFAULT:** A request for a copy of Notice of Default as defined in California Civil Code §2924b will be recorded. **If Not**, Seller is advised to consider recording a Request for Notice of Default.
9.* ☐ **REQUEST FOR NOTICE OF DELINQUENCY:** A request for Notice of Delinquency, as defined in California Civil Code §2924e, to be signed and paid for by Buyer, will be made to senior lienholders. **If not**, Seller is advised to consider making a Request for Notice of Delinquency. Seller is advised to check with senior lienholders to verify whether they will honor this request.
10.* ☐ **TAX SERVICE:**
   A. If property taxes on the Property become delinquent, tax service will be arranged to report to Seller. **If not**, Seller is advised to consider retaining a tax service, or to otherwise determine that property taxes are paid.
   B. ☐ Buyer, ☐ Seller, shall be responsible for the initial and continued retention of, and payment for, such tax service.
11. ☐ **TITLE INSURANCE:** Title insurance coverage will be provided to **both** Seller and Buyer, insuring their respective interests in the Property. **If not,** Buyer and Seller are advised to consider securing such title insurance coverage.
12. ☐ **HAZARD INSURANCE:**
   A. The parties' escrow holder or insurance carrier will be directed to include a loss payee endorsement, adding Seller to the Property insurance policy. **If not**, Seller is advised to secure such an endorsement, or acquire a separate insurance policy.
   B. Property insurance **does not** include earthquake or flood insurance coverage, unless checked:
   ☐ Earthquake insurance will be obtained; ☐ Flood insurance will be obtained.
13. ☐ **PROCEEDS TO BUYER:** Buyer will receive cash proceeds at the close of the sale transaction. The amount received will be approximately $_____, from _____ (indicate source of proceeds). Buyer represents that the purpose of such disbursement is as follows: _____.
14. ☐ **NEGATIVE AMORTIZATION; DEFERRED INTEREST:** Negative amortization results when Buyer's periodic payments are less than the amount of interest earned on the obligation. Deferred interest also results when the obligation does not require periodic payments for a period of time. In either case, interest is not payable as it accrues. This accrued interest will have to be paid by Buyer at a later time, and may result in Buyer owing more on the obligation than at its origination. The credit being extended to Buyer by Seller will provide for negative amortization or deferred interest as indicated below. (Check A, B, or C. CHECK ONE ONLY.)
   ☐ **A.** All negative amortization or deferred interest shall be added to the principal _____ (e.g., annually, monthly, etc.), and thereafter shall bear interest at the rate specified in the credit documents (compound interest);
   OR ☐ **B.** All deferred interest shall be due and payable, along with principal, at maturity;
   OR ☐ **C.** Other _____.

*(For Paragraphs 8-10) In order to receive timely and continued notification, Seller is advised to record appropriate notices and/or to notify appropriate parties of any change in Seller's address.

The copyright laws of the United States (Title 17 U.S. Code) forbid the unauthorized reproduction of this form, or any portion thereof, by photocopy machine or any other means, including facsimile or computerized formats. Copyright © 1997-2002, CALIFORNIA ASSOCIATION OF REALTORS®, INC. ALL RIGHTS RESERVED.

Buyer's Initials (_____)(_____)
Seller's Initials (_____)(_____)

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

Print

Property Address: _____ Date: _____

15. ☐ **ALL-INCLUSIVE DEED OF TRUST; INSTALLMENT LAND SALE CONTRACT:** This transaction involves the use of an all-inclusive (or wraparound) deed of trust or an installment land sale contract. That deed of trust or contract shall provide as follows:
A. In the event of an acceleration of any senior encumbrance, the responsibility for payment, or for legal defense is: _____ _____ ; OR ☐ **Is not** specified in the credit or security documents.
B. In the event of the prepayment of a senior encumbrance, the responsibilities and rights of Buyer and Seller regarding refinancing, prepayment penalties, and any prepayment discounts are: _____; OR ☐ **Are not** specified in the documents evidencing credit.
C. Buyer will make periodic payments to _____ (Seller, collection agent, or any neutral third party), who will be responsible for disbursing payments to the payee(s) on the senior encumbrance(s) and to Seller. **NOTE:** The Parties are advised to designate a neutral third party for these purposes.

16. ☐ **TAX IDENTIFICATION NUMBERS:** Buyer and Seller shall each provide to each other their Social Security Numbers or Taxpayer Identification Numbers.

17. ☐ **OTHER CREDIT TERMS** _____ _____

18. ☐ **RECORDING:** The documents evidencing credit (paragraph 3) will be recorded with the county recorder where the Property is located. **If not**, Buyer and Seller are advised that their respective interests in the Property may be jeopardized by intervening liens, judgments, encumbrances, or subsequent transfers.

19. ☐ **JUNIOR FINANCING:** There will be additional financing, secured by the Property, junior to this Seller financing. Explain: _____

20. **SENIOR LOANS AND ENCUMBRANCES:** The following information is provided on loans and/or encumbrances that will be **senior** to Seller financing. **NOTE:** The following are estimates, unless otherwise marked with an asterisk (*). If checked: ☐ A separate sheet with information on additional senior loans/encumbrances is attached

	1st	2nd
A. Original Balance	$ _____	$ _____
B. Current Balance	$ _____	$ _____
C. Periodic Payment (e.g. $100/month):	$ _____	$ _____/_____
Including Impounds of:	$ _____	$ _____/_____
D. Interest Rate (per annum)	_____%	_____%
E. Fixed or Variable Rate:	_____	_____
If Variable Rate: Lifetime Cap (Ceiling)	_____	_____
Indicator (Underlying Index)	_____	_____
Margins	_____	_____
F. Maturity Date	_____	_____
G. Amount of Balloon Payment	$ _____	$ _____
H. Date Balloon Payment Due	_____	_____
I. Potential for Negative Amortization? (Yes, No, or Unknown)	_____	_____
J. Due on Sale? (Yes, No, or Unknown)	_____	_____
K. Pre-payment penalty? (Yes, No, or Unknown)	_____	_____
L. Are payments current? (Yes, No, or Unknown)	_____	_____

21. **BUYER'S CREDITWORTHINESS:** (CHECK EITHER A OR B. Do not check both.) In addition to the loan application, credit report and other information requested under paragraph 2:
A. ☐ No other disclosure concerning Buyer's creditworthiness has been made to Seller;
OR B. ☐ The following representations concerning Buyer's creditworthiness are made by Buyer(s) to Seller:

Borrower	**Co-Borrower**
1. Occupation _____	1. Occupation _____
2. Employer _____	2. Employer _____
3. Length of Employment _____	3. Length of Employment _____
4. Monthly Gross Income _____	4. Monthly Gross Income _____
5. Other _____	5. Other _____

22. **ADDED, DELETED OR SUBSTITUTED BUYERS:** The addition, deletion or substitution of any person or entity under this Agreement or to title prior to close of escrow shall require Seller's written consent. Seller may grant or withhold consent in Seller's sole discretion. Any additional or substituted person or entity shall, if requested by Seller, submit to Seller the same documentation as required for the original named Buyer. Seller and/or Brokers may obtain a credit report, at Buyer's expense, on any such person or entity.

COPYRIGHT

Buyer's Initials (_____)(_____)
Seller's Initials (_____)(_____)

Copyright © 1997-2002, CALIFORNIA ASSOCIATION OF REALTORS®, INC.

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

SELLER FINANCING ADDENDUM AND DISCLOSURE (SFA PAGE 2 OF 3)

Print

Property Address: _____ Date: _____

23. CAUTION:

A. If the Seller financing requires a balloon payment, Seller shall give Buyer written notice, according to the terms of Civil Code §2966, at least 90 and not more than 150 days before the balloon payment is due if the transaction is for the purchase of a dwelling for not more than four families.

B. If **any** obligation secured by the Property calls for a balloon payment, Seller and Buyer are aware that refinancing of the balloon payment at maturity may be difficult or impossible, depending on conditions in the conventional mortgage marketplace at that time. There are no assurances that new financing or a loan extension will be available when the balloon prepayment, or any prepayment, is due.

C. If **any** of the existing or proposed loans or extensions of credit would require refinancing as a result of a lack of full amortization, such refinancing might be difficult or impossible in the conventional mortgage marketplace.

D. In the event of default by Buyer: (1) Seller may have to reinstate and/or make monthly payments on any and all senior encumbrances (including real property taxes) in order to protect Seller's secured interest; (2) Seller's rights are generally limited to foreclosure on the Property, pursuant to California Code of Civil Procedure §580b; and (3) the Property may lack sufficient equity to protect Seller's interests if the Property decreases in value.

If this three-page Addendum and Disclosure is used in a transaction for the purchase of a dwelling for not more than four families, it shall be prepared by an Arranger of Credit as defined in California Civil Code §2957(a). (The Arranger of Credit is usually the agent who obtained the offer.)

_____
Arranger of Credit - (Print Firm Name) By Date

Address _____ City _____ State _____ Zip _____

Phone _____ Fax _____

BUYER AND SELLER ACKNOWLEDGE AND AGREE THAT BROKERS: (A) WILL NOT PROVIDE LEGAL OR TAX ADVICE; (B) WILL NOT PROVIDE OTHER ADVICE OR INFORMATION THAT EXCEEDS THE KNOWLEDGE, EDUCATION AND EXPERIENCE REQUIRED TO OBTAIN A REAL ESTATE LICENSE; OR (C) HAVE NOT AND WILL NOT VERIFY ANY INFORMATION PROVIDED BY EITHER BUYER OR SELLER. BUYER AND SELLER AGREE THAT THEY WILL SEEK LEGAL, TAX AND OTHER DESIRED ASSISTANCE FROM APPROPRIATE PROFESSIONALS. BUYER AND SELLER ACKNOWLEDGE THAT THE INFORMATION EACH HAS PROVIDED TO THE ARRANGER OF CREDIT FOR INCLUSION IN THIS DISCLOSURE FORM IS ACCURATE. BUYER AND SELLER FURTHER ACKNOWLEDGE THAT EACH HAS RECEIVED A COMPLETED COPY OF THIS DISCLOSURE FORM.

Buyer _____ Date _____
(signature)

Address _____ City _____ State _____ Zip _____

Phone _____ Fax _____ E-mail _____

Buyer _____ Date _____
(signature)

Address _____ City _____ State _____ Zip _____

Phone _____ Fax _____ E-mail _____

Seller _____ Date _____
(signature)

Address _____ City _____ State _____ Zip _____

Phone _____ Fax _____ E-mail _____

Seller _____ Date _____
(signature)

Address _____ City _____ State _____ Zip _____

Phone _____ Fax _____ E-mail _____

THIS FORM HAS BEEN APPROVED BY THE CALIFORNIA ASSOCIATION OF REALTORS® (C.A.R.). NO REPRESENTATION IS MADE AS TO THE LEGAL VALIDITY OR ADEQUACY OF ANY PROVISION IN ANY SPECIFIC TRANSACTION. A REAL ESTATE BROKER IS THE PERSON QUALIFIED TO ADVISE ON REAL ESTATE TRANSACTIONS. IF YOU DESIRE LEGAL OR TAX ADVICE, CONSULT AN APPROPRIATE PROFESSIONAL.

This form is available for use by the entire real estate industry. It is not intended to identify the user as a REALTOR®. REALTOR® is a registered collective membership mark which may be used only by members of the NATIONAL ASSOCIATION OF REALTORS® who subscribe to its Code of Ethics.

SURE TRAC The System for Success™

Published by the
California Association of REALTORS®

Reviewed by _____ Date _____

EQUAL HOUSING OPPORTUNITY

SAMPLE

Comment: This form is reprinted with the permission of the California Association of Realtors®. Endorsement is not implied.

In addition to the information listed in this form, CC §2963 requires either a statement that a request for a notice of delinquency under CC §2924b has been made or, if no request has been made, a statement that the seller should consider making a request for a notice of delinquency.

The required disclosures (set forth in CC §2963(a)-(p)) must be given to the buyer by both the arranger of credit and the seller (information within the seller's knowledge), and to the seller by both the arranger of credit and the buyer (information within the buyer's knowledge). CC §2956.

No disclosure need be given to the buyer or the seller, however, when he or she is entitled to receive a disclosure under other disclosure laws set forth in CC §2958, such as the Federal Truth in Lending Act (see 15 USC §1604).

NOTE: The Board of Governors of the Federal Reserve System may exempt transactions and grant waivers from the Federal Truth in Lending Act. This raises a question of whether, if an exemption or waiver is granted and a party is no longer "entitled to receive" a federal truth in lending disclosure statement, the party then must receive a seller financing disclosure statement under CC §§2956-2957.

© The Regents of the University of California

III. SELLER-FINANCING DEVICES

§9.14 A. Installment Land Contract

Rather than securing the unpaid portion of the purchase price by a conventional security instrument such as a deed of trust (see §9.22), the parties may agree that the seller will retain legal title to the property until the buyer pays the balance of the purchase price. Under such an agreement, commonly known as an "installment land contract," the buyer holds equitable title and has the right to acquire legal title on completion of the contract. The contract affects the seller's legal title. Usually, possession of the property is transferred to the buyer on delivery of the contract, as are the risks of ownership. Although the seller does not receive a security interest in the property, retention of title operates in effect as security, and the installment land contract is therefore treated as a security device. *Venable v Harmon* (1965) 233 CA2d 297, 43 CR 490.

© The Regents of the University of California

§9.15 1. Distinguished From Purchase and Sale Agreement

Because the installment land contract is used as a security device, it must be distinguished from the purchase and sale agreement (see chap 4), under which legal title and possession are transferred to the buyer concurrently with payment of the purchase price. Under a purchase and sale agreement, any portion of the purchase price under the agreement not paid at close of escrow is typically represented by a promissory note, which is secured by a deed of trust, mortgage, or other security instrument. Further compounding the confusion over terminology, an installment land contract is called a "real property sales contract" in the Civil Code and is defined as an agreement to convey title on satisfaction of specified conditions, "which does not require conveyance of title within one year from the date of formation of the contract." CC §2985. This definition could include a purchase and sale agreement that does not require closing within 1 year, even though the parties do not intend the agreement to function as a security device.

© The Regents of the University of California

§9.16 2. Decline in Popularity; Disadvantages

The installment land contract was widely used in the early 1960s as an inexpensive and expedient financing vehicle. It also enjoyed some popularity in the 1970s as a device for circumventing due-on-sale clauses, based on the decision in *Tucker v Lassen Sav. & Loan Ass'n* (1974) 12 C3d 629, 116 CR 633. When the California Supreme Court extended *Tucker* to sales of property in which financing was evidenced by notes secured by deeds of trust in *Wellenkamp v Bank of America* (1978) 21 C3d 943, 148 CR 379, this rationale for using installment land contracts disappeared. The virtual overruling of *Wellenkamp* by the Garn-St. Germain Depository Institutions Act of 1982 (12 USC §1701j-3) has not led to a resurrection of the installment land contract, because the Garn Act probably supersedes *Tucker v Lassen* as well. See §§9.49-9.53 for discussion of due-on-sale clauses.

Before its brief resurgence in the 1970s, the installment land contract had gradually fallen into disfavor because of a series of court decisions that eliminated any legal advantage the contract offered sellers over a note secured by a deed of trust. See California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 1 (4th ed Cal CEB 2009) for a discussion of the judicial erosion of the seller's rights under installment land contracts. See also Graham, *The Installment Land Contract in California: Is It Really a Mortgage?*, 4 CEB Real Prop L Rep 117 (Oct. 1981).

Disadvantages of the installment land contract include the following:

- The applicability of CCP §580b, barring deficiency judgments (*Venable v Harmon* (1965) 233 CA2d 297, 43 CR 490);
- The existence of an equitable right of redemption under the contract, even for a willfully defaulting buyer (*Peterson v Hartell* (1985) 40 C3d 102, 219 CR 170; *MacFadden v Walker* (1971) 5 C3d 809, 97 CR 537; *Barkis v Scott* (1949) 34 C2d 116, 208 P2d 367; *Newhouse v Upchurch* (1971) 22 CA3d 204, 99 CR 436);
- The defaulting buyer's right to recover, as restitution, any amounts paid to the seller in excess of the seller's actual damages (*Freedman v The Rector* (1951) 37 C2d 16, 230 P2d 629); and
- The seller's inability to use an unlawful detainer action to evict a defaulting buyer who refuses to vacate the premises (*Greene v Municipal Court* (1975) 51 CA3d 446, 124 CR 139; CCP §1161).

Largely because of these disadvantages, the installment land contract is essentially obsolete as a security device in California in most financing transactions and should not be recommended as a financing method. However, the installment land contract is still used to some extent by developers of residential real estate lots.

© The Regents of the University of California

§9.17 3. Protective Statutory and Regulatory Provisions

A real property sales contract is defined in CC §2985 as an agreement to convey title, on satisfaction of specific conditions, that does not require conveyance within 1 year after the agreement's formation. See §§9.14-9.15. Under CC §2920(b), a real property sales contract is also considered a "mortgage" for purposes of CC §§2924-2924/ (nonjudicial foreclosure sales). Civil Code §§2985.1-2985.6 regulate these contracts and prohibit certain acts that might prejudice the seller's ability to convey unencumbered legal title to the buyer on completion of the contract. For example:

- CC §2985.4 restricts the seller's use of impound payments for insurance and taxes.
- CC §2985.5 requires that the contract contain certain information on tax payments and the contract term.
- CC §2985.6 permits the buyer to prepay the balance due under a contract for sale of land subdivided into a residential lot or lots containing a dwelling for no more than four families, except that the seller may prohibit prepayment for up to 12 months after the sale.

Regulations of the California Department of Real Estate applicable to the use of real property sales contracts in subdivision offerings require the seller to deposit the buyer's payments in an impound account until various conditions for the buyer's protection have been met. 10 Cal Code Regs §2791.9.

© The Regents of the University of California

B. Lease With Option to Purchase

§9.18 1. Reasons to Use

A prospective buyer can acquire possession but defer payment of the purchase price by using a lease with an option to purchase (known as a "lease-option"). This form of transaction is often used in the following circumstances:

- A home buyer is unable to meet a lending institution's standards for a loan (usually because the buyer lacks the 10- to 20-percent cash downpayment typically required by institutional lenders);
- A commercial lessee (including a ground lessee who has substantially improved the leased property) wants the right to purchase the property during the tenancy or at its end; or
- Market interest rates currently charged by institutional lenders are high and are expected to decline during the term of the lease-option.

In a typical lease-option, the option to purchase can be exercised at any time during the lease term. Because the market value of the property on the sale date may be higher than at the beginning of the lease term, the value of the option increases as its duration lengthens. To take account of inflation, the option price may sometimes be determined by an appraisal or by a formula using the consumer price index. Because the option is likely to become valuable over time and because the buyer-tenant is building "equity" through payment of the option consideration and rent (a portion of which is sometimes applied to the purchase price on exercise of the option), the courts may decline to strictly enforce landlord-tenant remedies that might lead to forfeiture of the option or may be lenient in granting relief from forfeiture under CCP §1179 or CC §3275.

PRACTICE TIP: To protect the interests of the tenant-optionee, the lease and the option agreement (or a memorandum of lease or option) should be recorded with the county recorder.

For more on lease-options, see Office Leasing: Drafting and Negotiating the Lease §§1.75, 23.8 (Cal CEB 1996).

© The Regents of the University of California

§9.19 2. Hidden Security Device

A lease-option may actually be intended as a security device for the lessor-optionor for a sale in which the seller retains title, rather than as a true lease with an option to purchase. Buyers and sellers have used the lease-option as a hidden security device to

- avoid exercise of a due-on-sale clause in an existing loan at a favorable interest rate (see §§9.49-9.53);
- avoid subordinating the seller's interest to the buyer's construction financing (see §§9.66-9.99);
- obtain favorable tax treatment (see Treas Reg §1.1234-1(a)-(b));
- avoid the effects of government regulations (*Frank Lyon Co. v U.S.* (1978) 435 US 561, 55 L Ed 2d 550, 98 S Ct 1291); or
- avoid statutory foreclosure requirements (see CC §§2924-2924*l*).

NOTE: A lease-option can also be used wrongfully. In *Garcia v Roberts* (2009) 173 CA4th 900, 93 CR3d 286, the buyer, who sought a loan to purchase the house he rented, was duped into allowing his purported lender to buy the property and then signed a lease-option document. The jury found fraud. Although, the substance of the case has to do with a procedural issue, the facts are illustrative of the misuse of the device.

© The Regents of the University of California

3. Distinguishing Lease-Option From Hidden Security Device

§9.20 a. How Courts Distinguish

In determining whether a lease-option is a hidden security device, a court will look to the parties' intent as evidenced by the agreement and the economic realities of the transaction. An important factor in determining whether a lease-option is a security device is a disparity between the purchase price when the option is exercised and the property's value. *In re San Francisco Indus. Park* (ND Cal 1969) 307 F Supp 271.

A lease-option will also constitute a security device if

- the rent payments are too high to be economically realistic; or
- the payments plus the option price closely approximate the fair market value of the property at the time of the agreement.

See *Robinson v Elliot* (9th Cir 1958) 262 F2d 383; *Haggard v Commissioner* (9th Cir 1956) 241 F2d 288; *Oesterreich v Commissioner* (9th Cir 1955) 226 F2d 798; Frank, *Lease With Purchase Option May Be Deemed Disguised Purchase If Caution Not Used*, 21 J Tax 66 (1964).

Apparently, the court will accept the parties' characterization of the transaction as a lease-option if the format is compelled by business or regulatory realities and not solely by tax-avoidance considerations. *Frank Lyon Co. v U.S.* (1978) 435 US 561, 55 L Ed 2d 550, 98 S Ct 1291.

© The Regents of the University of California

§9.21 b. How Tax Treatment Differs

If the transaction is treated as a true lease, the lessor is entitled to deduct depreciation, interest on mortgage loans, and other ordinary and necessary expenses of leasing the property (*Frank Lyon Co. v U.S.* (1978) 435 US 561, 55 L Ed 2d 550, 98 S Ct 1291), and rent payments are treated as ordinary income to the lessor, even though they may be applied to the purchase price on exercise of the option (*Joseph A. Harrah* (1958) 30 TC 1236).

If the property is commercial property used in the lessee's business, the lessee may deduct the rent payments as ordinary and necessary business expenses. See IRC §162. If the transaction is treated as a sale, the owner may be able to defer gain until the payments exceed basis (*Truman Bowen* (1949) 12 TC 446, acq 1951-2 Cum Bull 1) when the price is not ascertainable (see §9.38). The owner would not then be entitled to deduct depreciation and other amounts deductible by a lessor. *Frank Lyon Co. v U.S., supra*. Nor would a commercial lessee be entitled to deduct rent, but the lessee may be able to take depreciation deductions. On treatment of synthetic leases in which a lease is treated as a lease for financial accounting purposes but as a loan for federal income tax purposes, see Office Leasing: Drafting and Negotiating the Lease §§1.37A-1.37B (Cal CEB 1996).

If a lease-option is found to be a hidden security device, the rights and remedies of the parties on a breach of the agreement (for, *e.g.,* nonpayment of rent) are likely governed by the rules applicable to equitable mortgages (see California Mortgages, Deeds of Trust, and Foreclosure Litigation, chaps 3-5 (4th ed Cal CEB 2009)) and will not be terminable by a summary unlawful detainer proceeding.

© The Regents of the University of California

§9.22 C. Promissory Note Secured by Mortgage or Deed of Trust

The most common seller financing device is a promissory note for the unpaid portion of the purchase price, executed by the buyer in favor of the seller and secured by a lien that enables the seller to foreclose on the property if the buyer defaults. In many jurisdictions, the instrument securing the note is a mortgage, but in California the security instrument is usually a deed of trust. See generally California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 1 (4th ed Cal CEB 2009); California Real Estate Finance Practice: Strategies and Forms, chaps 3-4 (Cal CEB 2000).

All financing devices have the primary purpose of protecting the lender (in this instance, the seller) if the buyer fails to pay the purchase price. An installment land contract (see §§9.14-9.17) and a lease-option (see §§9.18-9.21) protect the seller by having the seller retain title to the property until the purchase price is paid. In contrast, under the note and security instrument method, the buyer receives title but gives the seller a recordable instrument, which encumbers the property and enables the seller to foreclose in case of default.

A transaction in which a seller "carries back" a note and deed of trust can be structured in many different ways. The seller may accept the entire purchase price in the form of a note. More often, the seller will require a partial cash downpayment. The seller may finance the balance of the purchase price or the buyer may pay a portion of the price with a new third party loan (or assumption of an existing encumbrance), and the seller will receive from the buyer a note secured by a second deed of trust for the balance of the purchase price. On institutional financing, see generally Real Estate Finance §§1.17-1.24. On seller financing with existing encumbrances, see §§9.41, 9.48-9.54. Important federal income tax benefits may inure to a seller who defers payment of the purchase price to later years. See §§9.24-9.39. If the property is to be developed, the buyer may need the seller to participate in financing the development by subordinating its interest to that of construction lenders (see §§9.66-9.99), by releasing portions of the property from the seller's lien as development progresses (see §§9.100-9.109), or both.

California regulates mortgages and deeds of trust extensively. On creation and form of security instruments, see CC §§2920-2944, 2947-2955.5. On foreclosure of security instruments, see CCP §§580a-580d, 725a-730.5; CC §§2924a-2924l.

© The Regents of the University of California

§9.23 D. Buyer's Obligation to Comply With FIRPTA

Under the Foreign Investment in Real Property Tax Act of 1980 (FIRPTA) (IRC §§897, 1445) (see §§15.80-15.84), the buyer is required to withhold a portion of the purchase price equal to 10 percent of the full amount realized by a foreign seller, including subsequent payments made under a promissory note or any other security instrument carried back by the transferor. IRC §1445(a); Treas Reg §1.1445-1(g)(5). When the initial cash paid by a buyer of a real property interest in the United States is not high enough to cover the withholding liability arising from the sale of the interest (*e.g.,* an installment sale), the buyer and the seller can request a "qualifying statement" from the Internal Revenue Service. A qualifying statement authorizes the buyer to withhold a lesser amount. IRC §1445(b)(4)(B). For a more extensive discussion of FIRPTA, see §§15.80-15.84.

California imposes a similar withholding requirement on sales by nonresidents of California. Rev & T C §§18649, 26131

© The Regents of the University of California

IV. POSTPONING SELLER'S INCOME TAX LIABILITY

§9.24 A. Installment Method of Reporting Gain

When payment of all or part of the purchase price will be received after the close of the tax year in which the sale occurs, IRC §453 requires that the transaction be treated as an installment sale, unless the seller elects not to use the installment method. For purposes of state taxation, California's treatment of installment sales for individuals conforms generally to federal law. Under the installment method, the seller pays taxes on the realized gain in the tax years that principal payments are received. Dealers in property, real or personal, are barred from reporting on the installment method (with limited exceptions). IRC §453(b)(2)(A). See §9.32. Installment sales under §453 must be distinguished from open transactions (those with a contingent sales price in which the fair market value of the buyer's obligation cannot be ascertained), under which no gain is reported until the property's basis has been recovered, at which point all future payments are reported as gain. See §9.38.

Although IRC §453 ordinarily requires that a qualifying sale be reported as an installment sale, a seller may elect out of the installment method of reporting and instead report the entire gain in the year of sale. IRC §453(d)(1). Except as otherwise provided, an election not to have the installment method apply to a particular disposition must be made on or before the due date (including extensions) for filing the income tax return for the year in which the sale occurs. IRC §453(d)(2); Temp Treas Reg §15A.453-1(d)(3)(i). The election, once made, can be revoked only with IRS consent. IRC §453(d)(3).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.25 1. Statutory Requirements; Definitions

§9.25 1. Statutory Requirements; Definitions

The installment method is used to report gains only, not losses. Installment Sales Revision Act of 1980 (Pub L 96-471, §2, 94 Stat 2247). At least one payment must be received in a tax year other than the year of sale. IRC §453(b)(1). The following definitions are important in calculation of gain:

- **"Taxable income"** is computed for any tax year by multiplying the payments received from the sale by the "gross profit ratio" for the sale:

  Amount Received in Tax Year × Gross Profit Ratio = Taxable Income

- **"Gross profit ratio"** equals the "gross profit" divided by the "total contract price":

$$\text{Gross Profit Ratio} = \frac{\text{Gross Profit}}{\text{Total Contract Price}}$$

- **"Gross profit"** equals the "selling price" minus the adjusted tax basis (to which commissions and selling expenses are added) of the property sold.
- **"Selling price"** equals the gross selling price without reduction for existing loans or expenses of sale.
- **"Total contract price,"** which is the denominator of the gross profit ratio, is computed by reducing the "selling price" by the amount of any loan encumbering the property that the buyer either assumes or takes subject to, or any loan that, if not secured by the property, is incurred or assumed by the buyer incident to the purchase of the property. (The limit of such indebtedness, however, is the seller's adjusted tax basis in the property. See example in §9.28 for situations in which the encumbrance is in excess of basis.)

In addition to cash payments in any given year, the computation of tax on any installment sale includes the following (Temp Treas Reg §15A.453-1(b)(3)):

- Evidence of indebtedness either from persons other than the purchaser or secured directly or indirectly by cash or a cash equivalent;
- Cancellation of any indebtedness of the seller to the buyer;
- Qualifying indebtedness assumed or taken "subject to" by the buyer in excess of the seller's basis in the property (but adjusted for selling expenses); or
- Evidence of indebtedness encumbering the property sold but for which the seller is not liable.

© The Regents of the University of California

2. Computation Examples

§9.26 a. Typical Installment Sale

The following are examples of typical installment sales:

EXAMPLE 1: An individual taxpayer sells an apartment building for $200,000, receiving a $50,000 downpayment and a $150,000 note secured by deed of trust, payable in 15 equal annual installments of $10,000 plus interest (interest is separately taxed at ordinary income rates) beginning January 1 of the year after the year of the sale. The adjusted basis in the property is $120,000. The current encumbrance, which will be paid at closing, is $30,000. The expenses of sale are $10,000. The tax consequences of the sale are computed as follows:

YEAR 1	
Gross Profit:	$200,000 − ($120,000 + $10,000) = $70,000
Total Contract Price:	$200,000 (face value of note plus downpayment)
Gross Profit Ratio:	$70,000 ÷ $200,000 = 35%
Taxable Income in Year of Sale:	$50,000 downpayment × 35% = $17,500

YEAR 2 and following	
Taxable Income:	$10,000 × 35% = $3500

The $30,000 encumbrance had no effect on the computation because it was paid off at closing.

EXAMPLE 2: If the $30,000 encumbrance had been assumed or taken subject to, the total contract price would have been reduced by $30,000 (as would, of course, the note given to the seller), and the computation would have been as follows:

YEAR 1	
Gross Profit:	$200,000 − ($120,000 + $10,000) = $70,000
Total Contract Price:	$200,000 (selling price) − $30,000 (encumbrance assumed) = $170,000 (face value of note plus downpayment)
Gross Profit Ratio:	$70,000 ÷ $170,000 = 41.18%
Taxable Income in Year of Sale:	$50,000 downpayment × 41.18% = $20,590

YEAR 2 and following	
Taxable Income:	$8000 × 41.18% = $3294 ($8000 is the annual installment on $120,000 installment note payable in 15 equal annual installments plus interest.)

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.27 b. Effect of Recapture

§9.27 b. Effect of Recapture

If the installment method is applied to a sale of real property involving recapture of all depreciation on "Section 1245 property" (generally depreciable personal property and property used in manufacturing, elevators, and escalators) and depreciation in excess of straight-line depreciation on "Section 1250 property" (generally buildings and leases), all "recapture income" must be reported in the year of disposition, whether or not any payment is received in that year. IRC §453(i). This additional increment of taxation is computed at ordinary income rates.

EXAMPLE: Use the same facts as in the first example in §9.26, but assume that $15,000 of depreciation is subject to recapture under IRC §1245 or §1250. This amount will be included in income in the year of the sale, but it will also be added back to the adjusted basis to find the gross profit on the remaining taxable gain.

YEAR 1	
Gross Profit:	$200,000 − ($120,000 + $10,000 + $15,000) = $55,000
Total Contract Price:	$200,000 (face value of note plus downpayment)
Gross Profit Ratio:	$55,000 ÷ $200,000 = 27.5%
Taxable Income in Year of Sale:	
(1) From downpayment:	$50,000 downpayment × 27.5% = $13,750
(2) Ordinary income from recapture:	$15,000

YEAR 2 and following	
Taxable Income:	$10,000 × 27.5% = $2750

© The Regents of the University of California

§9.28 c. Mortgage in Excess of Basis

Although significant economic benefits may be gained by refinancing, a seller whose encumbrances exceed adjusted basis at the time of sale will have to "pay the piper." Payments in the year of sale, therefore, equal the cash received *plus* the excess of the mortgage over the taxpayer's adjusted basis (when the encumbrance is assumed or taken subject to by the buyer). Temp Treas Reg §15A.453-1(b)(3)(i). The following example illustrates this:

EXAMPLE: Assume that the taxpayer has sold property for $100,000 with an adjusted basis of $30,000. The buyer assumes a $40,000 encumbrance, gives the seller a $10,000 downpayment and a note calling for principal payments (plus interest taxed as ordinary income) of $10,000 in each of the succeeding 5 years. The seller's expenses of sale are $4000.

Gross Selling Price	$100,000
Adjusted Basis	(30,000)
Selling Expenses	(4,000)
Gross Profit	$ 66,000
Selling Price	$100,000
Assumed Encumbrance ($40,000) *less* excess of Assumed Encumbrance over Adjusted Basis ($40,000 − $30,000) *plus* Selling Expenses ($4,000)	(34,000)
Total Contract Price	$66,000
Gross Profit Ratio	1:1

Thus, in the year of the sale, 100 percent of the $10,000 downpayment is taxable, plus the excess ($6000) of the encumbrance assumed over the sum of the taxpayer's adjusted basis and the selling expenses, *i.e.,* $34,000. This computation is in accord with *Kirschenmann v Commissioner* (9th Cir 1973) 488 F2d 270. In subsequent years, 100 percent of the principal payments are taxable.

© The Regents of the University of California

§9.29 3. Wraparound Financing

The "mortgage in excess of basis" problem may be avoided if the seller makes a sufficient principal payment before sale to eliminate the excess of debt over basis (or, of course, pays the loan off at closing). It has also been held that, if the mortgage is neither taken subject to nor assumed by the buyer, the excess of mortgage liabilities over basis is not a year-of-sale payment.

A common way to structure a transaction so that the buyer neither assumes, nor takes subject to, an existing encumbrance that is left on the property is through the use of wraparound financing. See §§9.56-9.65. With wraparound financing, the seller continues to pay on the underlying debt. Such an agreement is evidence that the buyer has neither assumed the mortgage nor taken the property subject to the mortgage, and therefore no payment in the amount of the excess mortgage has occurred within the meaning of Treas Reg §1.453-4(c). *Stonecrest Corp.* (1955) 24 TC 659, 667, nonacq 1956-1 Cum Bull 6. Any underlying debt that the seller continues to pay is disregarded for tax purposes.

The IRS took exception to this manner of reporting gain. In 1981, the IRS issued temporary regulations (Temp Treas Reg §15A.453-1(b)(3)(ii)) purporting to nullify the gain, and thus defeating the effect of the *Stonecrest* technique. In *Professional Equities, Inc.* (1987) 89 TC 165, the temporary regulations were invalidated by the unanimous ruling of the Tax Court in a case involving the use of an installment land sale contract. This result was followed in *Vincent E. Webb* (1987) TC Memo 1987-451, involving a wraparound mortgage.

© The Regents of the University of California

4. Seller's Ability to Limit Prepayments

§9.30 a. Restrictions on Limitations on Prepayment

Frequently, a seller will want to limit the amount received in the year of sale and in future years, either as part of the seller's tax planning or as part of an overall financial plan. The seller's ability to limit the buyer's payments is subject to restrictions, however, which must be carefully considered when structuring an installment sale. There is no right to prepay a note unless it is expressly permitted by either the note itself or a statute (see California Real Estate Finance Practice: Strategies and Forms §1.86 (Cal CEB 2000)), and California statutes do create this right in many real property sales. Civil Code §2954.9 permits prepayment at any time of a loan for residential property of four units or fewer when the loan is secured by a deed of trust, mortgage, or other lien on real property. Even if the property is unimproved when a note is executed, CC §2954.9 applies if both parties agree that the buyers will construct a principal residence on the property within 1 year of purchase and the buyers do so before payment of the prepayment fee. *Garver v Brace* (1996) 47 CA4th 995, 55 CR2d 220. Civil Code §2985.6 also expressly permits prepayment of real property sales contracts under certain circumstances.

A seller who takes back a security interest can restrict payments in the calendar year of sale under CC §2954.9(a)(3) if the seller does not take back four or more security instruments during the same calendar year. Thus, although the restrictions of §2954.9 may defeat income from being spread over several years, they should still permit a seller to limit payments during the year of the sale.

Civil Code §2954.11, containing provisions similar to CC §2954.9, applies to any installment loan secured by a deed of trust or mortgage or any other lien on residential property of four units or fewer to which CC §2954.9 does not apply. Section 2954.11 does not apply, however, to any loan that is subject to Bus & P C §10242.6 (prepayment penalty provisions applicable to single-family, owner-occupied dwellings).

A taxpayer using an accounting year other than the calendar year should note that §2954.9(a)(3) allows the seller to restrict prepayments only in the calendar year of sale.

EXAMPLE: If a seller on a July 1 to June 30 taxable year sells property in December, prepayments can be restricted only until the end of that calendar year, but the seller's taxable year extends another 6 months. Timing the sale to close in January would enable the seller to restrict prepayments for the remainder of the taxable year.

NOTE: Although legitimate prepayment penalties are enforceable, prepayment penalties that are intended as a delinquency (late-payment) penalty are not enforceable. *Ridgley v Topa Thrift & Loan Ass'n* (1998) 17 C4th 970, 73 CR2d 378.

© The Regents of the University of California

§9.31 b. Monetary Penalty on Prepayments

An alternative to barring prepayments altogether is imposing a monetary penalty on prepayments. Prepayment charges are permitted for loans for residential property of four or fewer units (CC §2954.9(a)(1)-(2)) but are limited in amount (CC §2954.9(b)). If the property is not residential property of four or fewer units, the only limitation on the prepayment charge is that it not be exorbitant or unconscionable. The seller can calculate the additional tax liability that a prepayment would entail and impose a penalty adequate to cover it. *Williams v Fassler* (1980) 110 CA3d 7, 167 CR 545 (penalty of 50 percent of any prepayment upheld on showing that additional tax amounted to 41 percent of prepayment).

© The Regents of the University of California

§9.32 5. Treatment of Dealers

"Dealer" property is that which is held primarily for sale to customers in the ordinary course of a trade or business (see IRC §1221(1)), in contrast with property that is held for use in a trade or business, for investment purposes, or as a principal residence. Gain on the sale of "dealer" property is not entitled to be taxed using the capital gains rates of taxation, which are generally lower than the rates for ordinary income. Currently the maximum rate at which ordinary income is taxed is 39.6 percent (IRC §1(a)-(e)), which is more than the current maximum capital gains rate. Dealers are also prohibited from using the installment method of reporting gain on the sale of "dealer" property, with limited exceptions, for sales made after January 1, 1988. IRC §453(*l*)(1)(B).

© The Regents of the University of California

§9.33 6. Disposition of Installment Obligations

A seller who contemplates selling an installment note must be aware that disposition of the note normally results in recognition of gain in the year of sale of the note. Unless exempted by statute or regulation, every sale or other "disposition" of an installment obligation results in recognition of gain to the holder of the obligation equal to the amount realized on disposition less the basis of the installment obligation. IRC §453B(a)(1). Because of the breadth of the term "disposition," careful analysis of the proposed transaction must be made if recognition of gain is to be avoided. Transfers such as outright sales, gifts, transfers in trust, cancellations, and so forth will generally be considered dispositions. If the installment obligation arising from a sale in which the price exceeded $150,000 is pledged, the net proceeds of the loan will be considered an installment sale payment as of the later of the time that either the debt is secured directly by any interest in the loan obligation or the loan proceeds are received by the taxpayer. IRC §453A(d). However, neither the seller's death nor various categories of liquidations and corporate reorganizations are considered dispositions.

© The Regents of the University of California

§9.34 7. Original Issue Discount and Imputed Interest

Buyers and sellers try to exploit the "time value of money," and this economic reality is reflected in the tax treatment of loans carried back in sales transactions. These laws are designed to prevent the distortions that occurred when sellers artificially increased the sales price of a property and reduced the interest rate on the indebtedness carried back by the seller, thus transmuting ordinary interest income into capital gain, which is taxed at a lower rate.

Both the Tax Reform Act of 1984 (Pub L 98-369, 98 Stat 494) and the Simplification Act of 1985 (Pub L 99-121, 99 Stat 505) address the issue of unstated interest (*i.e.,* the stated interest is lower than the minimum amount prescribed by statute). This problem is addressed by the Original Issue Discount (OID) rules of IRC §§1271-1275 and the imputed interest rules of IRC §483.

© The Regents of the University of California

§9.35 a. Original Issue Discount

Original Issue Discount (OID) is defined as the excess of an obligation's redemption price payable at maturity over its issue price. IRC §1273(a)(1). That is, OID is additional interest that has not been specifically provided for in the debt instrument.

In addition, the stated interest element in OID obligations should be compared with a safe harbor rate based on the applicable federal rate. See IRC §1274(c)(2)-(3). If interest is not stated at least at the safe harbor rate, interest is imputed at a higher rate based on the cost of federal funds. See IRC §1274(b).

The OID rules apply to a debt instrument with a maturity of more than 1 year given in consideration for the sale or exchange of property if some or all of the payments due under the debt instrument are due more than 6 months after the date of the sale or exchange and the redemption price payable at maturity exceeds either (1) the stated principal amount of the debt, if there is adequate stated interest, or (2) the sum of the present values of all payments due under the debt, using a discount rate based on the applicable federal rate. See IRC §§1272(a)(2)(C), 1274(c)(1), (3).

© The Regents of the University of California

§9.36 b. Imputed Interest Rules

The unstated interest rules of IRC §483 generally apply only to payments due more than 6 months after a sale or an exchange under a contract in which some or all of the payments are due more than 1 year after the sale or exchange. IRC §483(c)(1). Section 483 rules do not apply when the sale price is $3000 or less. IRC §483(d)(2).

The imputed interest rules of IRC §483 provide for a self-adjusting rate of interest tied to the cost of federal borrowing on obligations of similar maturities. The imputed interest rules apply only to the extent that the OID rules of IRC §1274 do not. IRC §483(d)(1). Section 1274 does not apply to the following:

- Any real property sale of $250,000 or less;
- The sale of one's principal residence;
- The sale of a farm by an individual, estate, testamentary trust, or defined small business corporation or similar partnership for a sales price of $1,000,000 or less;
- Intrafamily land sales to which IRC §483(e) applies;
- Obligations with a maturity of 1 year or less; or
- Certain other situations.

See IRC §§1272(a)(2)(C), 1274(c)(3). Internal Revenue Code §483(e) limits the discount rate used to determine total unstated interest in certain land transfers of $500,000 or less between family members. Neither §1274 nor §483 applies when a buyer assumes or takes subject to existing debt, unless the terms of that debt are modified. IRC §1274(c)(4).

© The Regents of the University of California

§9.37 c. Applicable Federal Rate

The test for imputing unstated interest or OID involves a comparison of the agreed rate of interest, based on the maturity date of the instrument, with federally designated short-, mid-, or long-term rates of interest called the Applicable Federal Rate (AFR). Debt instruments not over 3 years in length apply the short-term rate, those over 3 years but not over 9 years apply the mid-term rate, and those over 9 years apply the long-term rate. AFRs are recalculated monthly. If the test is not met, the interest rate will be held to be equal to the AFR and the terms of sale will be recharacterized accordingly. A simplified rule applies for sales involving a debt instrument of not more than $2,800,000 (indexed beginning in 1989), in which the imputed interest is limited to the greater of 9 percent compounded semiannually, or the AFR. See IRC §1274A(a)-(b).

© The Regents of the University of California

§9.38 B. Open-Ended or Contingent Sales Price

Occasionally, a sales price is not specified but is determined on the basis of future events. For instance, a subdivider may acquire land subject to a pricing formula that will ultimately fix the price based on the number of lots approved by a public agency. Such contingent-price sales must be reported under the installment method unless the seller elects out. Temp Treas Reg §15A.453-1(c)(1). Internal Revenue Code §453(g)(1)(B)(ii) and the implementing regulations prescribe several different ways of reporting gain in these cases.

When the maximum selling price can be ascertained, that price is treated as the "selling price" for purposes of applying normal installment sale calculations. If the maximum amount is later reduced, the gross profit ratio is recomputed in future years to achieve the correct result. Temp Treas Reg §15A.453-1(c)(2)(i)(A).

When the maximum selling price cannot be ascertained but the period of time over which the sale price is paid is known, the adjusted tax basis of the property is allocated in equal annual increments. Temp Treas Reg §15A.453-1(c)(3)(i). For the years in which no payment is received or the amount received exclusive of interest is less than the basis allocated for that year, no loss is allowed unless the taxable year is the final payment year under the agreement. Temp Treas Reg §15A.453-1(c)(3)(i). For those years, the unrecovered portion of the basis is carried forward to the next year. Temp Treas Reg §15A.453-1(c)(3)(i).

If neither the maximum selling price nor the payment period is known, the IRS may question whether the arrangement is a lease or a license rather than a sale (Temp Treas Reg §15A.453-1(c)(4)), but ultimately the taxpayer's basis will be held to be recovered in equal annual increments over a 15-year period if a sale is established to the satisfaction of the IRS. Temp Treas Reg §15A.453-1(c)(2)-(4).

The open-ended or contingent sales rules discussed above substantially reduce the justification for treating transactions as "open." Open transactions are accounted for by using the cost recovery method, under which no gain is realized until the basis is recovered. Its use should be limited to rare and extraordinary cases involving sales for a contingent price in which the fair market value of the purchaser's obligation cannot be reasonably ascertained. Installment Sales Revision Act of 1980 (Pub L 96-471, 94 Stat 2247). If the sale remains open, the payments are applied as received to reduce basis, and only when cumulative payments exceed basis is gain realized. Loss is recognized only when there is no likelihood of further recovery. *Burnet v Logan* (1931) 283 US 404, 75 L Ed 1143, 51 S Ct 550.

© The Regents of the University of California

§9.39 C. Relationship to Buyer's Financing Needs

The seller's desire to limit payments in the year of sale and spread the tax benefits over a number of years may conflict with the buyer's need to have land released from the seller's lien as development progresses (see §9.100). Negotiations on deferring payment must take into account factors such as subordination, financing and development needs, partial reconveyances, and release. The forms in §§9.45-9.46 offer suggestions for resolving these competing needs. See also §9.109 on substitution of security.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/ V. DEFERRING PAYMENTS; FORM PROVISIONS FOR PURCHASE AND SALE AGREEMENT/§9.40 A. Form: Cash Downpayment

V. DEFERRING PAYMENTS; FORM PROVISIONS FOR PURCHASE AND SALE AGREEMENT

§9.40 A. Form: Cash Downpayment

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§9.40-9.47.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

9.40-1 Cash downpayment

[*If appropriate, add to section 3.6 of the purchase and sale agreement (form 4.171-6)*]

Buyer shall make a cash downpayment of _ _[*dollar amount*]_ _ and shall deposit the downpayment into escrow in immediately available funds at least one business day before close of escrow.

[*Continue with provision in §9.41, §9.45, or §9.46*]

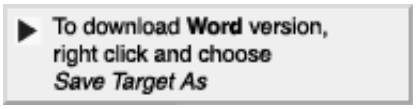
Comment: If all payments are to be made at close of escrow, this form should be used. If there are deferred payments, this form may be used with that in §9.45 or §9.46. If existing financing is to be retained (see §9.41), the precise balance of the financing retained may not be determined until closing, and the precise amount of the buyer's downpayment may similarly not be determined until the loan balance is established. In this case, the amount of the buyer's downpayment may need to be identified as an "approximate" amount to ensure that the downpayment, existing encumbrances, and seller financing (if any) total the exact purchase price.

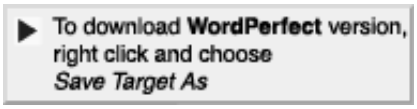
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.41 B. Form: Credit for Existing Encumbrances

§9.41 B. Form: Credit for Existing Encumbrances

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§9.40-9.47.





9.41-1 Credit for existing encumbrances

[*Insert after form 9.40-1, if appropriate*]

Buyer shall assume _ _[*or take title "subject to"*]_ _ **the existing promissory note in favor of** _ _[*name of lender*]_ _ **secured by** _ _[*e.g., a first*]_ _ **deed of trust against the property dated and recorded on** _ _[*date*]_ _**, as Instrument No.** _ _ _**, Official Records of** _ _[*name*]_ _ **County, and receive a credit toward the purchase price equal to the outstanding principal balance due. As of the execution of this agreement, the approximate outstanding balance of the existing encumbrance is** _ _[*dollar amount*]_ _**.** _ _[*Buyer/Seller*]_ _ **shall pay all assumption fees and costs incurred in Buyer's assumption of the existing encumbrance.**

Comment: When the buyer assumes or acquires title "subject to" existing encumbrance(s), the provision in §9.40 should be followed with this provision, which gives the buyer credit for principal still due on the retained encumbrance(s). See also §4.38 on retained encumbrances.

The parties should ascertain before close of escrow the balance due on prior encumbrances as well as other terms of the notes and security instruments. The buyer should not overlook accrued interest on prior encumbrances and should receive a credit for any accrued interest that is added to principal. Otherwise, interest on any existing financing should be prorated. The agreement should allocate liability for any other charges of the encumbrance, such as accrued late charges, foreclosure costs, assumption fees, impound accounts, and so forth. The parties should also look for prepayment penalties in the existing encumbrances. If the buyer is to assume responsibility for any prepayment penalty in the future (thus allowing the seller to avoid the penalty), the buyer may desire compensation for taking on this liability.

For rights of parties on assumption of encumbrances or taking property subject to them, see §§9.48-9.65. For sales in which the existing encumbrance is government financed or insured (*i.e.,* by the VA or the FHA), see §9.54.

© The Regents of the University of California

C. Promissory Note for Balance Due

§9.42 1. Form of Loan Documents

Forms of the note and deed of trust to be used should be attached to the purchase and sale agreement to avoid later disputes about their terms. Unless the exact form of the note is attached, the note submitted at close of escrow may or may not provide for attorney fees, grace periods, late charges, allocation of payments between principal and interest, an acceleration clause (see §9.47), or other terms not contemplated by the parties and not discussed during negotiations. If the deed of trust is not attached, the instrument actually submitted might contain restrictions on the buyer's use of the property, or other uncontemplated provisions, although this is unlikely if a standard title company form is used.

Forms for notes and deeds of trust are usually available from title companies, although it is often better for the attorney to draft the note because many of its provisions will be unique to that transaction. A title company deed of trust form will often need some modification and require an addendum. The note and deed of trust must be modified to include the special provisions that the parties have negotiated, such as acceleration of principal (see §9.47), subordination (see §§9.66-9.99), and release and reconveyance of land (see §§9.100-9.110). These provisions can be duplicated from the agreement itself as addendums to the deed of trust. All-inclusive notes and deeds of trust are discussed in §§9.56-9.65.

PRACTICE TIP: From the seller's perspective, caution should be exercised in using standard title company deeds of trust for substantial transactions because these forms often contain inadequate lender protections, especially on the lender's rights to collect rents, liens on personal property, and due-on-sale language.

© The Regents of the University of California

§9.43 2. Security; Title Insurance

When the security for the buyer's note is property other than that conveyed, the nature of the security (*e.g.,* a first deed of trust) should be stated and an exact list of all prior encumbrances given by reference either to an exhibit or to a preliminary report. The seller should obtain a lender's title insurance policy covering the stated priority of the security, together with a statement from the holder or the beneficiary of each itemized encumbrance having priority, as provided in CC §2943. If the security instrument encumbers all or part of the property sold, for clarity its priority should be stated, even though priority can be ascertained from other provisions in the agreement. Title insurance should likewise be obtained by the seller, and the agreement should specify who pays the title insurance premium. On title insurance for lenders, see generally California Title Insurance Practice, chap 8 (2d ed Cal CEB 1997).

© The Regents of the University of California

§9.44 3. Computation of Payments

Payments under the seller's note may be computed in different ways. The payment amounts may remain constant, with the amounts applied to principal and interest varying according to an amortization schedule. This method is the one usually adopted for purchases of residential property. Another method provides for payment of principal in equal installments plus interest either on the unpaid balance or on the payment due. Seller carryback notes also commonly require interest-only payments, with the principal balance due on maturity. Finally, seller financing will sometimes provide for all or part of the interest to be deferred until a specified date or until maturity. When interest is deferred, the agreement and note must specify whether the deferred interest is compounded (*i.e.,* whether it bears interest) and, if so, how frequently (*e.g.,* monthly), and once periodic payments are commenced whether they are calculated on the original principal balance of the note or the balance increased by the deferred interest. Most (but by no means all) seller-carryback notes, even those calling for payments based on a 15- or 30-year amortization schedule, will require a balloon payment.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.45 4. Form: Note for Balance; First-Year Payments Limited

§9.45 4. Form: Note for Balance; First-Year Payments Limited

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§9.40-9.47.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

9.45-1 Note for balance (first-year payments limited)

[*Precede with form 9.40-1; see alternative provision, note for balance, in form 9.46-1*]

The balance of the purchase price of _ _[*approximately/exactly*]**_ _ _ _**[*dollar amount*]**_ _ shall be evidenced by a promissory note executed by buyer in favor of seller, in the form attached hereto as Exhibit _ _, bearing interest at _ _ percent per annum, _ _**[*principal and*]**_ _ interest payable in _ _**[*annual/monthly*]**_ _ installments, beginning on _ _**[*or before*]**_ _ _ _**[*date*]**_ _, and continuing on _ _**[*or before*]**_ _ the _ _**[*e.g., tenth*]**_ _ day of each _ _**[*e.g., month*]**_ _ thereafter until paid with the balance of the note payable _ _**[*e.g., 5 years*]**_ _ after close of escrow; as long as payments of principal within 1 year after close of escrow do not exceed _ _**[*dollar amount*]**_ _.**

Buyer's note is to be secured by _ _[*e.g., a first deed of trust*]**_ _ in the form _ _**[*used by _ _*[*name of title company or lender*]**_ _ _ _**[*as modified*]**_ _**]**_ _ in the form attached as Exhibit _ _, _ _**[*encumbering the property/(describe other security property)*]**_ _.**

Comment: The note may permit the buyer to make larger payments than those provided for in the note by

- specifying periodic payments of a stated amount "or more"; or
- requiring payments to be made "on or before" specified dates.

When the first method is used, payments in excess of the stated amount may not be applied to the next succeeding installment when due but must be applied to reduce either previously accrued interest or the outstanding principal balance. *Smith v Renz* (1954) 122 CA2d 535, 265 P2d 160. If the second method is used, as suggested in the form, excess payments may be directed by the buyers to satisfy succeeding installments. See CC §1479 on specifying application of payments made by a debtor who is under several obligations to the same creditor. If no right to prepay is specified, the note may not be prepaid (*Smiddy v Grafton* (1912) 163 C 16, 124 P 433) unless a statutory right of prepayment exists (see, *e.g.,* CC §§2954.9, 2954.11 (residential loans); CC §1916.5(a)(5) (variable rate loans); Bus & P C §10246.6 (broker-arranged loans); 12 CFR §590.4(5) (residential manufactured housing loans regulated by Office of Thrift Supervision); 24 CFR §200.87 (FHA loans); 38 CFR §36.4310 (VA loans); and Mil & V C §987 (Cal-Vet loans)).

The form limits prepayment during the first year after sale in order to preserve installment sale treatment. The purchase price must be paid in *more than 1 year* to qualify for installment sale treatment. There is no longer a rule restricting the percentage that can be paid in the first year after the sale. An alternative to limiting the amount that can be prepaid in the year following the sale is to prohibit any prepayment in the year of the sale. See §§9.30-9.31. Deletion of the last clause of the first paragraph will result in a fully prepayable note.

Civil Code §2954.9 permits prepayment of a loan secured by owner-occupied residential property of four units or fewer, and the agreement cannot prevent prepayment for sales of such property. Prepayment charges are permitted, but CC §2954.9(b) restricts their amount on loans secured by a mortgage or deed of trust on owner-occupied residential property containing four or fewer units. Civil Code §2954.11 contains similar provisions applicable to any installment loan secured by a deed of trust or mortgage or any other lien on residential property of four residential units or fewer to which CC §2954.9 does not apply. Civil Code §2954.11 does not, however, apply to any loan that is subject to Bus & P C §10242.6 (prepayment penalty provisions applicable to single-family, owner-occupied dwellings). See §§9.30-9.31. Prepayment must be allowed for residential transactions (and first loans of $20,000 or less and second loans of $10,000 or less (Bus & P C §10242.6)), and penalties may be imposed only on prepayments exceeding 20

percent of the original balance in any year during the first 5 years.

In nonresidential situations, absolute prohibitions on prepayment (known as "lock-in" provisions) are enforceable (CC §2954.9), as are reasonable prepayment penalties. See *French v Mortgage Guar. Co.* (1940) 16 C2d 26, 104 P2d 655; *Sacramento Sav. & Loan Ass'n v Superior Court* (1982) 137 CA3d 142, 186 CR 823; *Williams v Fassler* (1980) 110 CA3d 7, 167 CR 545; Stark, *Enforcing Prepayment Charges: Case Law and Drafting Suggestions*, 22 ABA Real Prop Prob & Trust J 549 (Fall 1987); California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 8 (4th ed Cal CEB 2009) (on prepayment). In development situations, the buyer often expects land to be released as payments are made, making the release provisions of the agreement closely related to installment payment provisions. For release provisions, see §§9.100-9.110. For another form for seller financing, see section 2.4 of the purchase and sale agreement (form 4.170-4).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.46 5. Form: Note for Balance; Annual Payments Limited

§9.46 5. Form: Note for Balance; Annual Payments Limited

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§9.40-9.47.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

9.46-1 Note for balance (annual payments limited)

[*May be substituted for form 9.45-1 for balance owed to seller*]

The balance of the purchase price of _ _[*approximately/exactly*]_ _ _ _[*dollar amount*]_ _ **shall be evidenced by a promissory note executed by Buyer in favor of Seller, in the form attached as Exhibit** _ _**, bearing interest at** _ _ **percent per annum, due** _ _[*number*]_ _ **years after the date of close of escrow. The note shall require** _ _[*e.g., monthly/annual*]_ _ **installments of principal and interest in the amount of** _ _[*dollar amount*]_ _ **beginning on** _ _[_ _[*e.g., June 15, 2000*]_ _ *and on the* _ _[*e.g., 15th*]_ _ *day of each month thereafter until June 15, 2010/*_ _[*e.g., February 1, 2000,*]_ _ *and on the* _ _[*e.g., first day of each February*]_ _ *thereafter until* _ _[*e.g., February 1, 2010*]_ _]_ _**.**

Buyer's note is to be secured by _ _[*e.g., a first deed of trust*]_ _ **in the form** _ _[*used by* _ _[*name of title company or lender*]_ _ *attached as Exhibit* _ _]_ _**, encumbering** _ _[*specify property conveyed or describe other property*]_ _**. Buyer may prepay up to** _ _ **percent of the original principal balance in any 12-month period commencing no sooner than** _ _[*date*]_ _**, on giving Seller** _ _[*e.g., 30 days' written notice* _ _[*and on paying to Seller a prepayment premium of* _ _ *percent of the amount prepaid*]_ _]_ _**.**

Comment: The seller may want payments spread over as long a period as possible for reporting gain (see §9.24), while the buyer may desire flexibility to pay the seller's note early. This form is a compromise, with a minimum and a maximum prepayable for each year. After reaching the annual maximum, the buyer may wish to have land released or to be permitted to substitute other security for the land after the maximum is reached and still receive the benefit of additional partial reconveyances of land. For a form permitting substitution of security, see §9.109. For variations in the method of paying interest and limitations on prepayment prohibitions and penalties, see §9.44.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.47 D. Form: Acceleration on Default

§9.47 D. Form: Acceleration on Default

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§9.40-9.47.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

9.47-1 Acceleration on default

[*If appropriate, add to section 3.6 of the purchase and sale agreement (form 4.171-6)*]

The note shall contain the following provision:

If the maker defaults on the payment of principal, interest, or any other sum required under this note when due, or in the performance of any of the agreements in the deed of trust securing this note, or if an involuntary bankruptcy petition is filed against the maker under the United States Bankruptcy Code that is not dismissed within 60 days or if the maker files a voluntary bankruptcy petition under the United States Bankruptcy Code,

[*Add if there is a prior encumbrance*]

or if the maker fails to make payments required by any encumbrance having a priority of record to the deed of trust securing this note or to perform any obligation under such encumbrance or otherwise allows any such encumbrance to be in default,

[*Continue*]

the entire principal balance plus accrued interest, if any, shall immediately become due and payable, without notice, at the option of the holder of this note.

Comment: All installment note forms provide for acceleration of the unpaid balance on default in payment of any installment of principal or interest or performance of any covenant in the deed of trust. If the installment note is attached to the purchase and sale agreement, acceleration provisions should be incorporated in the note and need not be repeated in the agreement. Any changes in a printed form note should be initialed by both parties. The acceleration clause should also appear in the security instrument, which if recorded gives constructive notice to all subsequent purchasers and lien holders. See CC §1214. The definition of actions constituting a default under the security instrument is often broader than that in the note. See California Real Estate Finance Practice: Strategies and Forms, chap 4 (Cal CEB 2000).

Other actions giving the payee the right to accelerate may include selling or further encumbering the property. The latter will be enforceable only in commercial transactions. See §§9.49-9.53 on due-on-sale clauses. This form provides that the seller may declare a default and accelerate the note if the buyer files a voluntary bankruptcy case or is the subject of an involuntary bankruptcy case. The commencement of a bankruptcy case gives rise to an "automatic stay" under 11 USC §362 that prohibits a creditor from taking any action to enforce a debt against the bankrupt party or from enforcing any lien against property of the bankrupt party. However, the "automatic stay" does not apply to protect any guarantor or co-obligor on the note. See *In re Chugach Forest Prods., Inc.* (9th Cir 1994) 23 F3d 241. Thus, the default-on-bankruptcy language is included to permit action against any guarantor or endorser or co-maker in the event of a bankruptcy of one of the makers.

A defaulting trustor or his or her successor may reinstate the obligation by curing most monetary defaults up until 5 business days before a trustee's sale held under a power of sale, or before entry of judgment of foreclosure. CC §§2924c, 2924e. See California Mortgages, Deeds of Trust, and Foreclosure Litigation, chaps 2-3 (4th ed Cal CEB 2009). The beneficiary under a subordinate deed of trust or a person holding a subordinate lien may also reinstate under CC §2924c by paying the amount in default plus costs and expenses at any time during the period commencing

with the date of recordation of the notice of default until 5 business days before the date of a trustee's sale set forth in the initial recorded notice of trustee's sale or, if the sale is postponed for more than 5 business days, until 5 business days before the date of the postponed sale.

© The Regents of the University of California

VI. RETAINING EXISTING ENCUMBRANCES

§9.48 A. Buyer's Assumption of, or Sale Subject to, Existing Encumbrances

Assuming or taking title subject to an existing encumbrance may permit the buyer and the seller to avoid prepayment penalties and refinancing costs and to retain an existing encumbrance with a favorable interest rate. The terms of the existing financing (including the interest rate, payment terms, and prepayment rights) should be examined by the buyer and compared with those available with new financing. The all-inclusive note and deed of trust is yet another approach to retaining existing encumbrances (see §§9.56-9.65).

A buyer who merely takes title subject to an existing encumbrance is a "nonassuming grantee" and does not become personally liable for the underlying obligation. *Cornelison v Kornbluth* (1975) 15 C3d 590, 125 CR 557. The lender retains the property as security for payment of the obligation and may hold the original borrower personally liable for a deficiency judgment only if a deficiency judgment is available to the lender. (If the obligation is a purchase-money obligation under CCP §580b, the lender may not hold the borrower liable for any deficiency even if the borrower waived the protection of §580b (*DeBerard Props. v Lim* (1999) 20 C4th 659, 85 CR2d 292) or if the borrower otherwise promised to remain liable on the loan (*Lawler v Jacobs* (2000) 83 CA4th 723, 100 CR2d 52; see also *Cadle Co. II v Harvey* (2000) 83 CA4th 927, 100 CR2d 150).

A nonassuming buyer will, however, be personally liable for waste resulting from intentional or reckless conduct and, in the absence of a CCP §580b defense, may also be liable for waste resulting from negligent conduct. *Cornelison v Kornbluth, supra;* Leipziger, *The Mortgagee's Remedies for Waste*, 64 Cal L Rev 1086, 1129 (1976). (However, if the creditor submits a full credit bid at a foreclosure sale on the subject property, it would not be able to recover damages for waste. *Michelson v Camp* (1999) 72 CA4th 955, 85 CR2d 539.)

The buyer may also assume an existing loan by written agreement with either the lender or the seller. In the latter case, a specific recital of assumption in the deed constitutes a sufficient writing (CC §1624(a)(6)), and the assuming buyer becomes personally liable to the beneficiary for repayment of the loan under a theory of equitable subrogation (*Braun v Crew* (1920) 183 C 728, 192 P 531). On assumption generally, see also California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 9 (4th ed Cal CEB 2009); on CCP §580b and exceptions to it, see Mortgage Deed of Trust Foreclosure, chap 5.

Without any express provisions, the seller remains liable under the original obligation. However, the seller's liability is that of a guarantor and will be subject to defenses that are available to a guarantor. See §§4.38-4.43. If the seller desires to be released from liability on the encumbrance being assumed, an assumption agreement in which the lender specifically releases the seller is necessary.

For a more detailed description of assumption of and sale subject to existing encumbrances and their interaction with California antideficiency legislation, see Mortgage Deed of Trust Foreclosure, chap 9.

© The Regents of the University of California

§9.49 1. Due-on-Sale and Due-on-Encumbrance Clauses

A due-on-sale clause in the existing note and deed of trust may limit the new buyer's ability to take subject to or to assume the obligation. A due-on-sale clause permits the secured lender to accelerate the loan in the event of a sale or other specified transfer or transaction affecting the property. See California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 8 (4th ed Cal CEB 2009).

© The Regents of the University of California

a. Enforceability of Clauses

§9.50 (1) Due-on-Sale Clauses

Although California law previously restricted the lenders' rights to enforce due-on-sale (*Wellenkamp v Bank of America* (1978) 21 C3d 943, 148 CR 379) and due-on-encumbrance clauses (*La Sala v American Sav. & Loan Ass'n* (1971) 5 C3d 864, 97 CR 849), the enactment of the Garn-St. Germain Depository Institutions Act of 1982 (the Garn Act) (Pub L 97-320, 96 Stat 1469) made such clauses generally enforceable. Section 341 of the Garn Act (12 USC §1701j-3) preempts all state law, including judicial decisions limiting or restricting enforcement of due-on-sale clauses in real property loans, and provides that enforcement of those clauses be governed exclusively by the terms of the loan contract secured by the real property. 12 USC §1701j-3(b)(1)-(2).

The Federal Home Loan Bank Board issued regulations (12 CFR §§591.1-591.6) on May 13, 1983, implementing Garn Act §341. For a discussion of these regulations and their impact on due-on-sale clauses in California, see Rader, *The Federal Home Loan Bank Board Issues Final Regulations to Implement the Due-on-Sale Provision of the Garn-St. Germain Act*, 6 CEB Real Prop L Rep 93 (July 1983).

© The Regents of the University of California

§9.51 (2) Due-on-Encumbrance Clauses

In addition to validating the enforceability of due-on-sale clauses, the Garn-St. Germain Depository Institutions Act of 1982 (12 USC §1701j-3) and the implementing regulations (12 CFR §§591.1-591.6; see §9.50) have validated due-on-encumbrance clauses except in certain residential transactions that are expressly exempt from enforcement. However, the original Garn Act contained an exception to enforceability of a due-on-encumbrance clause in the case of junior financing. The Federal Home Loan Bank Board's implementing regulations limited this exception to owner-occupied residential dwellings. The validity of these regulations was initially questioned because the Garn Act's exception was not so limited. Congress later accepted the FHLBB's limitation, however, and amended the Garn Act to provide that personal residences—and only personal residences—are exempt from enforcement of due-on-encumbrance clauses in the event junior financing was placed against the security property. 12 USC §1701j-3(d). This limitation apparently authorized the enforcement of due-on-encumbrance clauses in commercial loans.

© The Regents of the University of California

§9.52 b. Prohibition on Prepayment Penalties

Under the Garn-St. Germain Depository Institutions Act of 1982 §341 (12 USC §1701j-3), a lender may not impose a prepayment penalty or equivalent fee for, or in connection with, loan acceleration by exercise of a due-on-sale clause when the real property security is an owner-occupied residence. 12 CFR §591.5(b)(2). Depending on the wording of the prepayment penalty clause, the imposition of a prepayment penalty may also be prohibited following a due-on-sale acceleration of a loan entered into before Garn Act §341 was enacted. See *Tan v California Fed. Sav. & Loan Ass'n* (1983) 140 CA3d 800, 189 CR 775.

After the decision in *Tan,* CC §2954.10 was enacted to prohibit a lender from charging a prepayment fee following acceleration of any loan secured by real property, by the exercise of a due-on-sale clause, unless the parties have waived the provisions of §2954.10. The borrower and the lender may agree to waive §2954.10 if the property is nonresidential real property or residential real property containing more than four units, and the borrower may agree to pay a prepayment penalty on acceleration under a due-on-sale clause. The waiver must be separately signed or initialed by the borrower and "its enforcement shall be supported by evidence of a course of conduct by the obligee of individual weight to the consideration in that transaction for the waiver or agreement." CC §2954.10. The Federal Home Loan Bank Board issued similar regulations under the Garn Act in 1985, prohibiting the collection of a prepayment charge on acceleration of a due-on-sale clause in a mortgage or deed of trust encumbering an owner-occupied dwelling. 12 CFR §591.5(b)(2). There are no reported cases addressing whether CC §2954.10 is preempted by the Garn Act.

Civil Code §2954.11 permits a borrower, at any time, to wholly or partially prepay with interest an "installment loan" as defined, secured by a deed of trust or mortgage or any other lien on residential property of four or fewer units. It also provides that a borrower may be obligated to pay a prepayment charge, with stated limitations, when prepaying within 5 years of the date the loan was made.

© The Regents of the University of California

§9.53 c. Impact on Buyer

Because due-on-sale (and, in most cases, due-on-encumbrance) clauses are fully enforceable, the buyer who wishes to retain an existing loan must pay close attention to the provision in the existing loan documents. Many institutional loans have due-on-sale clauses but provide for assumption by a creditworthy purchaser. Usually, an assumption fee is charged. If the buyer and the seller elect to proceed with a sale "subject to" the existing loan without applying for formal assumption despite the existence of due-on-sale clause, the seller should insist on a provision in the sale contract that indemnifies the seller for liability to either the buyer or the lender in the event the due-on-sale clause is enforced. The seller should also insist on a provision that the indemnification shall survive the close of escrow and remain in effect for the number of years remaining on the loan. The all-inclusive note and deed of trust are sometimes used in an attempt to camouflage a transaction that entitles the lender to accelerate under the due-on-sale clause, although this attempt may not succeed, because lenders tend to rely on notices concerning insurance coverage, rather than noting who actually makes the payments, in order to ascertain a change of ownership.

In a transaction in which the existing loan is retained and the seller takes a junior note and deed of trust for a portion of the purchase price, the buyer and the seller will need to pay close attention to the prohibitions on further encumbrances in the underlying loan documents. If the buyer applies for a formal assumption and the loan contains a due-on-encumbrance clause, the assumption documents should specifically address and consent to the junior loan from the seller, as well as consent for the sale to the buyer.

Even if a deed of trust authorizes a lender to accelerate a loan under a due-on-sale clause, that right may have been waived. *Rubin v Los Angeles Fed. Sav. & Loan Ass'n* (1984) 159 CA3d 292, 205 CR 455 (lender accepted payments from new buyer for 2 years with full knowledge of transfer and without any reservation of rights).

If the parties propose to use an option in connection with the transaction, it should be recognized that a true option by itself should not be deemed to violate a due-on-sale provision in any deed of trust. Despite the recent claims of certain large financial institutions, case law makes it clear that an option is merely an offer. See *Beakins Moving & Storage Co. v Prudential Ins.* (1985) 176 CA3d 245, 253, 221 CR 738. An option creates a contract right in the offeree. *Hudson Props. Co. v Governing Bd.* (1985) 168 CA3d 63, 72, 213 CR 909. That right is in personam for the option holder. *Pacific S.W. Dev. Corp. v Western Pac. R.R.* (1956) 47 C2d 62, 66, 301 P2d 825. An option is not an interest in real property. *Warner Bros. Pictures v Brodel* (1948) 31 C2d 766, 772, 192 P2d 949; *Anthony v Enzler* (1976) 61 CA3d 872, 876, 132 CR 553. It does not give the optionee any estate in real property. *Leslie v Federal Fin. Co* (1939) 14 C2d 73, 80, 92 P2d 906; *Southern Christian Leadership Conf. v Al Malaikah Auditorium Co.* (1991) 230 CA3d 207, 222, 281 CR 216. An option by itself does not result in any change in interest, title, or possession of real property. *Vierneisel v Rhode Island Ins. Co.* (1946) 77 CA2d 229, 232, 175 P2d 63.

© The Regents of the University of California

§9.54 2. Transferability of Government Financing

Existing encumbrances may include loans guaranteed by the Veterans Administration (VA) (38 USC §§3701-3714), loans insured by the Federal Housing Administration (FHA) under the National Housing Act (12 USC §§1701-1750g), or loans made by the State of California through the Department of Veterans Affairs (Mil & V C §§985-989.9) (Cal-Vet loans provide for lower interest rates and downpayments than do conventional loans). Loans guaranteed by the VA, for which commitments were made before March 1, 1988, are transferable, although the original borrower remains liable unless released by the VA. 38 USC §3713. VA-guaranteed loans for which commitments were issued on or after March 1, 1988, and loans closed on or after January 2, 1989, may be assumed, although such assumptions require credit approval of the purchaser. 38 USC §3714(f). Loans insured by the FHA that originated before December 15, 1989, are transferable. FHA loans that originated on or after December 15, 1989, are subject to credit approval of the purchaser and the payment of authorized assumption fees. 12 USC §1709(g), (r), as amended by Pub L 101-235, 103 Stat 1987, 2026. Written consent of the Department of Veterans Affairs is required to transfer Cal-Vet loans (Mil & V C §987.1), but assumption is rare because a purchaser who is acceptable to the Department of Veterans Affairs can usually obtain a larger loan in his or her own right, and on assumption the seller loses the right to a second Cal-Vet loan (Mil & V C §987.16).

© The Regents of the University of California

§9.55 3. Impact of Antideficiency Laws

The practitioner must be aware of the continuing protection of CCP §580b in any situation involving a transfer of the real property or of the debt. A purchaser who acquires property subject to a purchase-money loan or who assumes a purchase-money loan is entitled to the protection of §580b. See *Frangipani v Boecker* (1998) 64 CA4th 860, 75 CR2d 407. This protection cannot be circumvented by having the parties sign new documents if there are no material changes to the original loan documents. *DMC, Inc. v Downey Sav. & Loan Ass'n* (2002) 99 CA4th 190, 120 CR2d 761. Moreover, if a purchase-money loan is assigned to a third party, §580b continues to protect the maker despite the assignment. See *Costanzo v Ganguly* (1993) 12 CA4th 1085, 16 CR2d 55; California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 5 (4th ed Cal CEB 2009).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.55A 4. Restrictions on Foreclosure

§9.55A 4. Restrictions on Foreclosure

In 2008 and 2009 the California Legislature enacted CC §§2923.5-2923.52, which imposed certain restrictions on foreclosure on owner-occupied residential property securing loans made during 2003-2007. Civil Code §2923.5 prohibits recording a notice of default until the lender has satisfied certain notice and restructure requirements. Civil Code §2923.52 imposes an additional 90-day period before the lender may record a notice of sale unless the lender has qualified for an exemption under CC §2923.53. However, both of these statutes apply only to first-priority liens. As a result, a seller who takes a junior secured lien on residential property will have greater foreclosure rights than a first-priority lien holder which made its loan during the designated period.

© The Regents of the University of California

B. All-Inclusive Note and Deed of Trust

§9.56 1. Definition

The all-inclusive deed of trust, sometimes referred to as "wraparound," or "overriding," is a real property security device used for secondary financing. The terms "all-inclusive deed of trust" and "all-inclusive note" will be used in this text to refer to the deed of trust and promissory note used in an all-inclusive loan.

When used in seller financing, an all-inclusive deed of trust is similar to a conventional second deed of trust, except that the indebtedness represented by the all-inclusive note includes both the deferred portion of the purchase price and the unpaid balance of a promissory note secured by a prior encumbrance. With conventional secondary seller financing, the buyer would assume or take subject to the prior encumbrance.

EXAMPLE: If property encumbered by a first deed of trust securing a promissory note with an unpaid balance of $40,000 is to be sold for $60,000, with a downpayment of $10,000, the seller could take back a note for $10,000 secured by a second deed of trust, or an all-inclusive note for $50,000. The all-inclusive deed of trust will contain the seller's covenant to pay the principal and interest installments accruing on the senior note.

Although the all-inclusive deed of trust may be used for third party as well as seller financing, the discussion in §§9.57-9.65 is limited to seller financing. For discussion of the wraparound deed of trust in third party financing, see Lane, *The "Wrap-Around" Mortgage: Tax Problems Related to its Use in Connection with the Refinancing or Sale of Real Estate*, 33 NYU Inst Fed Tax 1235 (1975). See also California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 9 (4th ed Cal CEB 2009). Unless otherwise indicated, the discussion in §§9.57-9.65 assumes the existence of only one prior encumbrance, although an all-inclusive deed of trust and all-inclusive note may wrap around and include any number of prior encumbrances and the obligations they secure.

© The Regents of the University of California

2. Purposes and Uses

§9.57 a. Higher Effective Interest Rate

The primary reason for using all-inclusive instruments is to allow both the buyer and the seller to take advantage of a lower interest rate on the existing loan.

EXAMPLE: If the interest rate on the existing first deed of trust is 6 percent, an all-inclusive second deed of trust at 8 percent will often (depending on the amount of the seller's equity in the wrapped note) generate far more interest for the seller than would a conventional second deed of trust, even at 10 percent, because the wraparound generates interest on the entire principal balance, not merely the additional funds.

Although a seller generally demands a purchase price in excess of the property's cash value as consideration for taking back a conventional second deed of trust, the buyer frequently gets a lower purchase price with wraparound financing because of the higher effective yield received by the seller. The wraparound arrangement may also result in smaller monthly payments than would be required for independent notes covering two unconsolidated loans. See California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 9 (4th ed Cal CEB 2009). On usury considerations, see §§9.6-9.7 and Mortgage Deed of Trust Foreclosure, chap 9.

© The Regents of the University of California

§9.58 b. Reporting Interest for Tax Purposes

It is unclear whether a seller should report the gross interest received under an all-inclusive note or the net after excluding interest on the underlying first deed of trust for income tax purposes. Some authority exists for reporting the gross amount of the interest received. Lane, *The "Wrap-Around" Mortgage: Tax Problems Related to its Use in Connection with the Refinancing or Sale of Real Estate*, 33 NYU Inst on Fed Tax 1235, 1243 (1975). The manner in which interest income is reported may affect an individual seller's basis for charitable contributions and a corporate seller's status as a subchapter S corporation or a personal holding company. 33 NYU Inst on Fed Tax at 1243. Whether the interest received is reported on a gross or a net basis will not affect the seller's taxable income.

© The Regents of the University of California

§9.59 c. Seller's Control Over Security

A seller who remains liable for making the payments on the existing senior lien retains greater control over the security and is assured that payments are made as due. See 4 Miller & Starr, California Real Estate §§10:22-10:23 (3d ed 2000). The buyer incurs a corresponding loss of control unless the all-inclusive note provides for payments to be made by the buyer to a third party disbursing agent. Use of such a third party collection agent, however, may cause the seller to realize taxable gain in a sale in which the encumbrances exceed the seller's adjusted basis in the property, because the transaction might be treated as including an assumption of the existing encumbrance by the buyer (see §9.60). See *Floyd J. Voight* (1977) 68 TC 99, aff'd (5th Cir 1980) 614 F2d 94; *Paul Trans Dang,* TC Memo 1999-233; Comment, *The Wrap-Around Mortgage: A Critical Inquiry*, 21 UCLA L Rev 1529, 1551 (1974). In any event, the buyer can obtain some protection by requiring the seller to furnish proof of payment of the underlying note each month and by recording a request for notice of default on the underlying note.

Sometimes buyers and sellers mistakenly believe that an all-inclusive note can be used to avoid a due-on-sale clause in the senior note. While the seller continues to make the payments on the senior note, theoretically the lender would never discover a transfer of the property. This is not a safe assumption, however, because lenders often discover sales by changes in insurance (showing the new buyer as a named insured) or tax records. Some lenders even employ services that check for property transfers. If the parties insist on using an all-inclusive note when the underlying note is due on sale, the buyer and the seller should allocate responsibility for the cost of refinancing if it becomes necessary, and the seller should also agree to subordinate its deed of trust to any such new financing.

© The Regents of the University of California

§9.60 d. Tax Considerations; Installment Reporting

The Installment Sales Revision Act of 1980 (Pub L 96-471, 94 Stat 2247) eliminated the requirement that payments in the year of sale be limited to 30 percent of the total sale price. See §9.25. Therefore, any encumbrance on the property, whether or not in excess of basis, will not affect the seller's ability to qualify for installment reporting, and this particular rationale for wraparound financing no longer applies. However, the excess of encumbrances over the seller's adjusted basis will be treated as a cash payment to the seller in the year of sale unless the seller uses wraparound instruments to be able to defer reporting that excess. See *Stonecrest Corp.* (1955) 24 TC 659, nonacq 1956-1 Cum Bull 6; *Professional Equities, Inc.* (1987) 89 TC 165, invalidating Temp Treas Reg §15A.453-1(b)(3)(ii). For further discussion of the tax consequences of all-inclusive instruments, see §9.29.

© The Regents of the University of California

§9.61 3. Drafting All-Inclusive Instruments

The all-inclusive deed of trust and the all-inclusive note must be drafted carefully, not only to achieve the benefits discussed in §§9.57-9.60 but to conform to the terms of the underlying first deed of trust and the note it secures. In addition, the all-inclusive deed of trust and the note must contain provisions satisfactory to the institutional trustee and to the title company that may be asked to conduct the trustee's sale and to insure title following delivery of a trustee's deed. Standard form deeds of trust customarily used in California are inadequate for this purpose and must be modified and supplemented. Some title companies have their own forms of the all-inclusive note and all-inclusive deed of trust. These forms should only be used after careful review and, if needed, modification. For an extensive discussion of drafting considerations, see Caplan, *The Wrap-Around Merry-go-round*, 1 Real Prop News 1 (Summer 1980).

The note and deed of trust must be drafted with the needs of the parties to the specific transaction in mind. Because these needs vary so greatly, it is difficult to draft all-purpose wraparound forms. It is possible, however, to pinpoint issues that must be addressed in drafting any wraparound instrument.

© The Regents of the University of California

§9.62 a. Consistency With Underlying Obligations and Encumbrances; Prepayments; Amortization

The most important point in drafting all-inclusive instruments is that they be consistent with the terms and provisions of the underlying note and deed of trust to ensure that the buyer's obligations and the seller's rights are not less than those of the maker and the payee under the underlying note.

EXAMPLES: Any event that constitutes a default or that permits acceleration of the first note should also be a default or permit acceleration under the all-inclusive note. If the underlying note contains a late charge provision, a similar provision should be added to the all-inclusive note and the wraparound deed of trust.

The seller may wish to schedule payments on the all-inclusive note enough in advance that the seller need not suffer out-of-pocket costs to make the payments on the underlying note and will also have time to pursue collection if the buyer does not pay on time.

Prepayment restrictions are a separate issue to be negotiated. If the underlying debt is locked in, with prepayments prohibited, the all-inclusive note and deed of trust should either prohibit prepayment or specify that prepayment is limited to the seller's equity in excess of the underlying debt. The buyer who has the right to prepay under the all-inclusive note may want to include a requirement that the seller execute a reconveyance when the unpaid balance of the all-inclusive note equals the balance on the senior note. The seller, however, may want the note to provide that the seller will continue to realize the interest differential even though his or her equity has been reduced to zero. If prepayment is to be permitted, the parties must decide how any prepayment is to be allocated between the wraparound and the underlying obligations. They must also decide who is to pay any prepayment charges incurred under the underlying note.

Payments on the all-inclusive note must be established after consideration of amortization schedules for both the note and the underlying debt, to ensure that the balance on the all-inclusive note will, throughout its life, exceed the balance on the underlying note. If the all-inclusive note is amortized faster than the underlying note, the principal balance of the underlying obligation could eventually exceed the balance on the all-inclusive note. When the underlying note is amortizing and the all-inclusive note is interest-only or is amortizing more slowly, the parties must allocate the benefit of the principal reduction on the underlying note to either the lender or the borrower.

© The Regents of the University of California

§9.63 b. Rights in Case of Default

The rights of each party if the other party defaults should be clearly spelled out. For example, most all-inclusive notes make the seller's covenant to make payments on the underlying note conditional on the buyer's performance of his or her obligations under the all-inclusive instruments. This condition seems an essential protection for the seller, who otherwise might be contractually obligated to continue paying on the underlying obligation despite the buyer's default on the wraparound. The buyer, however, needs protection against the seller's failure to make payments on the underlying note. This is frequently accomplished by providing that the buyer may make payments directly to the holder of the first deed of trust when the seller fails to do so, and that those payments will be credited against the next installments due under the all-inclusive note. The buyer might also require the seller to submit proof of payment within a specified time after the due date of each installment on the underlying obligation, or simply secure an agreement from the holder of the underlying encumbrance to send notice of a default. In any event, the buyer should include in the wraparound deed of trust, or separately record, a request for notice of default and notice of sale under CC §2924b. With the use of an installment land contract, it is a criminal offense for the seller to fail to properly apply the installment payments to the existing encumbrance. CC §2985.3. No similar provision exists, however, to compel the seller who takes back an all-inclusive note to pay on the underlying indebtedness.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.64 c. Foreclosure

§9.64 c. Foreclosure

Provisions regarding foreclosure under wraparound instruments are extremely important because many title companies will neither act as trustee nor insure title unless foreclosure provisions are clearly set forth. Questions arise because the trustor's payments on the all-inclusive note include amounts due on the underlying obligation:

- Does the holder of the wraparound deed of trust declare a default on both obligations or only on the installments due on the all-inclusive note?
- Does the holder bid the amount of the holder's equity or the full amount due on the wraparound at the trustee's sale?

Because the holder of the wraparound is obligated to pay on the included encumbrance, the wraparound instruments should provide that failure to pay on the wraparound is a default on that obligation only. The documents should provide that the purchaser at the trustee's sale acquires only the seller's equity, and therefore takes title subject to the senior lien.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.65 4. Form: Provision in Purchase and Sale Agreement for All-Inclusive Financing

§9.65 4. Form: Provision in Purchase and Sale Agreement for All-Inclusive Financing

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

9.65-1 Provision in purchase and sale agreement for all-inclusive financing

[*Precede with form 9.40-1*]

The balance of the purchase price shall be evidenced by an all-inclusive promissory note executed by Buyer in the form attached, secured by an all-inclusive deed of trust in the form attached, and bearing interest at _ _[*number*]_ _ percent per year, principal payable in _ _[*e.g., 12*]_ _ equal _ _[*annual/monthly*]_ _ installments, beginning on _ _[*date*]_ _, and continuing until the principal and interest due have been paid.

The total principal amount of the all-inclusive note shall include the unpaid principal balance of the following underlying promissory note(s) secured by deed(s) of trust:

(1) (a) Promissory note:

Maker:_____

Payee:_____

Date:_____

Original amount:_____

Unpaid balance:

(b) Deed of trust:_____

Beneficiary:_____

Original amount:_____

Recordation date:_____

Document No. _ _ _ _ _ _ Book: _ _ _ _ _ _ Page: _ _ _ _ _ _

Place of recordation: _ _ _ _ _ _ County, California

[*Repeat as necessary for each note and deed of trust*]

Comment: Drafting a provision for the purchase agreement is obviously simplified if the forms for the wraparound instruments have been agreed on and can be attached. If they are not available, key provisions to be included in the all-inclusive instruments should be specified in the purchase agreement itself. On drafting considerations, see §§9.61-9.64.

© The Regents of the University of California

VII. SELLER'S PARTICIPATION IN BUYER'S FINANCING

§9.66 A. Subordination

In addition to deferring a portion of the purchase price, the seller may be asked to assist in financing the buyer's development of the property either by subordinating the seller's purchase money deed of trust to liens for construction or permanent financing or by releasing portions of the property from the purchase money deed of trust as payments are made on it.

By subordinating his or her lien, the seller agrees that it will become junior in priority to the encumbrance to which it is subordinated, generally a lien for construction financing. Because the seller's security is at risk for successful completion and operation of the project, the seller will often require additional protection such as a lien on other property owned by the buyer or an increased purchase price. If the buyer intends to subdivide the security property or the property consists of multiple lots, it may be important to negotiate releases in addition to the subordination to enable the buyer to sell lots free of encumbrances as they are developed. See §§9.100-9.110.

© The Regents of the University of California

1. Subordinating to Construction Loans

§9.67 a. Competing Factors

When a developer buys land for subdivision or construction, the problem arises of financing both the land purchase and the construction. Two factors create a problem:

- A deed of trust securing a note for the purchase price of the land is given statutory priority over other liens, subject to the provisions of the recording acts (CC §2898; see *DMC, Inc. v Downey Sav. & Loan Ass'n* (2002) 99 CA4th 190, 199, 120 CR2d 761 (purchase money lien has priority over all other liens, even liens prior in time, because purchase money financing enables buyer to acquire subject property)); and
- Institutional lenders that normally furnish construction loans usually insist that they be secured by a first lien on the property.

Some institutional lenders may even be required to obtain a first lien. See, *e.g.,* Fin C §§1227 (state-licensed commercial banks), 1560 (trust companies). National banks are regulated by the Comptroller of the Currency and have more latitude than state banks. See 12 USC §371(a). Savings and loan associations, both federally chartered and state licensed, generally have more latitude in their lending activities. See, *e.g.,* 12 USC §1464(c)(1)(B). For discussion of the real estate lending regulations pertaining to state and federal banks and savings and loan associations, see California Real Estate Finance Practice: Strategies and Forms §1.19 (Cal CEB 2000).

© The Regents of the University of California

§9.68 b. Methods of Providing First Lien

The buyer-developer can provide the institutional construction lender a first lien by doing either of the following:

- Recording the construction loan deed of trust at the close of escrow before recording the seller's purchase money deed of trust (see §9.69); or
- Obtaining the seller's consent to subordinate the seller's lien to the lien securing construction financing when obtained (see §9.70).

The effect of subordination is to change the order of priority of the liens, which is created by the recording acts. Although an agreement on the order of recording security instruments at close of escrow is not truly a subordination agreement, both types of agreements may be treated by the courts as subordination agreements, and the rights and obligations of the construction lender and the seller may be treated similarly regardless of how their respective loan priorities are achieved. *Middlebrook-Anderson Co. v Southwest Sav. & Loan Ass'n* (1971) 18 CA3d 1023, 96 CR 338; see California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 9 (4th ed Cal CEB 2009); 5 Miller & Starr, California Real Estate §§11:193-11:194, 11:197 (3d ed 2000).

© The Regents of the University of California

§9.69 (1) Order of Recordation

Because a construction loan is not usually obtained until all development approvals are received and building permits are issued, the construction deed of trust is often recorded after recordation of the seller's deed of trust, and sometimes a significant time period elapses before the construction deed of trust is recorded. Similarly, permanent (or "take out") loans typically replace the construction financing after completion of the project and long after the seller's deed of trust was recorded (although it is not unusual for the permanent financing to pay the seller's note in full).

© The Regents of the University of California

§9.70 (2) Automatic Subordination; Subordination Agreement

Subordination may be accomplished automatically if the seller's deed of trust includes a provision that subordinates the lien of the deed of trust to those of the construction loan, the permanent loan, or both. Subordination may also be achieved by using a separate, recorded subordination agreement. Institutional lenders and title companies almost universally require that a change in order of priority be obtained by a separate subordination agreement, rather than by an automatic subordination provision in a deed of trust. See 5 Miller & Starr, California Real Estate §11:187 (3d ed 2000).

© The Regents of the University of California

§9.71 c. Risks to Seller

Following subordination to a construction loan, the property will generally be over-encumbered during the construction period because the total amount of the liens will exceed the value of the property until the improvements are completed. The seller receives some protection from the fact that most construction loans are disbursed by the lender in the form of progress payments as improvements are built and the value of the property theoretically increases correspondingly. See 5 Miller & Starr, California Real Estate §11:186 (3d ed 2000). However, these protections are not expressly for the benefit of the seller, and the seller cannot rely on the lender's enforcement.

A seller's interests may also be protected by making sure that the subordination agreement restricts the terms of the construction loan so that the proceeds may only be used to pay for improvements on the property. See §9.78. But see *Swiss Prop. Mgmt. Co. v Southern Cal. IBEW-NECA Pension Plan* (1997) 60 CA4th 839, 70 CR2d 587 (under terms of subordination agreement, lender not obligated to supervise disbursement of loan proceeds on behalf of subordinated seller). See §9.85.

When buyers default, few sellers are able either to take over and complete an unsuccessful real property development or to meet the payment obligations on the construction loan in order to prevent foreclosure of the senior lien. Some institutional lenders require that the contractor obtain a completion bond, giving additional protection for completion of construction for both the construction lender and the seller who holds a junior lien. The seller may want to condition subordination on the contractor posting such a bond even if the construction lender does not require it. If the construction loan is foreclosed, the buyer may be insolvent despite being personally liable for repayment of the seller's note. See *Spangler v Memel* (1972) 7 C3d 603, 102 CR 807; §9.95. Many practitioners recommend against subordination by a seller who is not a sophisticated real estate developer because of the many pitfalls for sellers (and their attorneys). See *Starr v Mooslin* (1971) 14 CA3d 988, 92 CR 583.

© The Regents of the University of California

§9.72 d. Seller's Benefits

In deciding whether to subordinate, the seller must consider (in addition to the purchase price) these factors:

- The developer's financial strength and ability;
- The economic potential of the proposed development;
- The availability of reserves to cover cost overruns and periods of high vacancies; and
- The state of the real property market.

Sellers will normally agree to accept the risks of subordination only in exchange for some benefit, such as a higher purchase price. In *Spangler v Memel* (1972) 7 C3d 603, 613, 102 CR 807, the court noted that the seller's agreement to subordinate made it possible to obtain the financing required to realize the commercial potential of the property, which in turn justified the higher purchase price (and, in a subordinating construction loan, the elimination of the buyer's purchase money antideficiency protection under CCP §580b). See also *Jack Erickson & Assocs. v Hesselgesser* (1996) 50 CA4th 182, 57 CR2d 591. In *DeBerard Props. v Lim* (1999) 20 C4th 659, 85 CR2d 292, however, the supreme court held that agreement to subordinate must in fact be acted on, *i.e.,* there must be an actual subordination to a construction loan that reduces the property's value at the time of sale. Moreover, the amount of the construction loan must be significant relative to the purchase price of the property. See *Lawler v Jacobs* (2000) 83 CA4th 723, 100 CR2d 52.

© The Regents of the University of California

§9.73 2. Types of Subordination Agreements

Subordination agreements are frequently classified as either executory or executed. An executory agreement (see §§9.74-9.82) is a mere promise by the seller to execute a subsequent subordination instrument. An executed subordination agreement may be either an automatic subordination agreement, as discussed in §9.86, or an executory agreement that became executed by the seller's actions in signing and recording a subordination instrument. Executed subordination agreements are discussed in §§9.83-9.87.

© The Regents of the University of California

§9.74 a. Executory Subordination Agreement

An executory subordination agreement is a promise by the seller to execute a subsequent instrument subordinating the seller's lien to the lien of a later loan. See *Handy v Gordon* (1967) 65 C2d 578, 55 CR 769; *Magna Dev. Co. v Reed* (1964) 228 CA2d 230, 39 CR 284. An executory agreement may be contained in a purchase and sale agreement, may be part of the seller's deed of trust, or may be a separate agreement.

PRACTICE TIP: The best practice (from the buyer's perspective) is to make the subordination agreement a part of or an addendum to the deed of trust so that any subsequent transferee of the note and deed of trust will clearly have notice of and be bound by the agreement. For further discussion and forms, see §§9.75-9.82. In addition, if the buyer has identified the prospective construction lender, that lender should review and approve the form of the subordination agreement.

© The Regents of the University of California

§9.75 (1) Enforceable: Certain and Reasonable

When the seller has made an executory agreement to subordinate the purchase money lien, the most important legal concern to the buyer is whether the buyer will be entitled to specific performance to compel the seller to carry out the seller's promise to subordinate. To be enforceable, an executory subordination agreement must be both certain and reasonable. *Handy v Gordon* (1967) 65 C2d 578, 55 CR 769. Often, the seller's subordination covenants are set forth in the purchase and sale agreement in addition to being made a part of the seller's deed of trust. If the subordination provision is unenforceable, the entire purchase and sale agreement is unenforceable (absent a severability clause), even if the buyer attempts to waive the subordination provisions. *Handy v Gordon, supra; Magna Dev. Co. v Reed* (1964) 228 CA2d 230, 39 CR 284.

The detailed terms of the subordinating loan must be stated if the agreement is to be sufficiently certain to be enforced specifically (*Handy v Gordon, supra*), and the terms of the subordination agreement must be just and reasonable to the seller (CC §3391(2)). In *Handy*, the California Supreme Court held that the agreement must define and minimize the risk that the subordinating liens will impair or destroy the seller's security. The court criticized several aspects of the purchase and sale agreement:

- The failure to limit the size and number of lots into which the property was to be subdivided;
- The lack of restrictions on the use of loan funds (leaving the possibility that funds might be used for purposes other than improvements, thus depleting the buyer's equity);
- The low downpayment ($100, which was insufficient to cushion the seller's position); and
- The deferral of any payment of principal to the seller until 3 years after close of escrow.

Decisions after *Handy* demonstrate the courts' willingness to deny both specific performance and damages under executory subordination agreements, particularly when enforcement is sought against unsophisticated sellers. See *Butcher v Dauz* (1967) 257 CA2d 524, 65 CR 166; *Spellman v Dixon* (1967) 256 CA2d 1, 63 CR 668; *Loeb v Wilson* (1967) 253 CA2d 383, 61 CR 377.

Compare *Woodworth v Redwood Empire Sav. & Loan Ass'n* (1971) 22 CA3d 347, 99 CR 373, in which specific performance was granted even though the loan terms were not specified in the subordination provisions, because the seller was an active participant in the financing and development, with *Ray Thomas Enters. v Fox* (1982) 128 CA3d 361, 180 CR 253, in which the court upheld a subordination provision in an agreement for purchase of a mobilehome park even though it did not state the terms of the institutional loan to be taken out by the purchaser. The court distinguished *Handy* on these grounds:

- The loan to be obtained was a purchase money loan rather than a construction loan; and
- There was sufficient equity to protect the holder of the note.

See also *Schneider v Ampliflo Corp.* (1983) 148 CA3d 637, 196 CR 172, in which the court distinguished *Handy* and held that foreclosure was an available remedy even though specific performance was not.

© The Regents of the University of California

§9.76 (2) Required Terms

To meet the test of certainty (see §9.75), the subordination agreement must specify the maximum principal of the new loan, maximum interest rate, maximum term, and mode of payment. *Cummins v Gates* (1965) 235 CA2d 532, 45 CR 417. To meet the additional test of fairness and reasonableness to the seller (*Handy v Gordon* (1967) 65 C2d 578, 55 CR 769), the agreement should include provisions that limit the terms of the new loan and the disbursement of its proceeds, including the following:

- The minimum repayment term, as well as the maximum, to avoid a burdensome balloon payment that the buyer might be unable to meet (see 5 Miller & Starr, California Real Estate §11:190 (3d ed 2000)).
- The purpose of the loan, what costs are to be paid from the loan proceeds, and the requirement that the loan funds be used only to construct improvements on the property or other specified uses (*Weiss v Brentwood Sav. & Loan Ass'n* (1970) 4 CA3d 738, 84 CR 736; *Ruth v Lytton Sav. & Loan Ass'n* (1968) 266 CA2d 831, 72 CR 521).
- The amount of loan fees and other charges, such as prepayment penalties, and other material provisions of the note and deed of trust to be delivered to the lender (charges amounting to 13.5 percent of the total loan have been held excessive in the absence of a provision for them (*Collins v Home Sav. & Loan Ass'n* (1962) 205 CA2d 86, 22 CR 817)). One solution is to specify permitted charges (*e.g.,* all costs of obtaining the loan or discounts, including loan fees, appraisers' charges, and escrow and title insurance fees) and set a maximum for them. Interest payments during the construction loan period and other indirect construction costs such as construction bond and insurance premiums, real property taxes during the construction loan period, leasing commissions, and legal expenses are sometimes also specified with appropriate limitations as to amount.
- If applicable, a description of the improvements to be constructed on the property (*Handy v Gordon, supra*).

When subordinating to a construction loan, the seller might also insist on assurances that the buyer has a firm commitment for take-out or permanent financing. *Jones v Sacramento Sav. & Loan Ass'n* (1967) 248 CA2d 522, 56 CR 741. Often, agreements will provide for subordination to take-out financing, as well as construction financing. The terms of the permanent financing should also be specified. See §9.81.

© The Regents of the University of California

§9.77 (3) Form: Optional Terms

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§9.77-9.82.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

Other terms of the subordinating loan that might be specified are the following:

Land improvement costs. The following is an example of a provision detailing the permitted charges for construction of a residential subdivision:

9.77-1 Optional terms: land improvement costs

(a) Actual construction costs of the dwelling with the usual appurtenances, including garage, patio, driveway, and fencing, but including expenditures only for labor and materials by Buyer or by an entity owned in whole or in part by Buyer;

(b) A prorata share of aggregate costs of general subdivision improvements, which shall consist of engineering fees, architectural fees, drafting fees, permit and inspection fees, map recording charges, subdivision bond premiums, on-site and off-site grading and excavation costs, and all costs for improvements required by the City of _ _[*name*]_ _ for approval of a subdivision map. The prorata share for each lot in the subdivision shall be determined by dividing each of the foregoing costs by the number of lots for which each cost is incurred.

Developer's fee. If the subordinating construction loan includes a distribution to the buyer-developer for a development or construction supervision fee, the subordination agreement should state this. See *Collins v Home Sav. & Loan Ass'n* (1962) 205 CA2d 86, 22 CR 817. Similarly, if the buyer will act as the general contractor, a specific provision for payment of a fee to the borrower as the general contractor should be included.

Purchase price of land. The subordination agreement should state whether loan proceeds may be applied to the purchase price of the land. *Radunich v Basso* (1965) 235 CA2d 826, 45 CR 824.

Other charges. The subordination agreement should describe any other charges that may be payable. In *Ruth v Lytton Sav. & Loan Ass'n* (1968) 266 CA2d 831, 72 CR 521, the interest rate of the construction loan was subject to increase from 6.75 percent to 8.75 percent on default. The court held that the loan did not comply with the conditions of the subordination agreement, which limited the interest rate to 7.2 percent.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.78 (4) Form: Executory Subordination Provision in Purchase Agreement

§9.78 (4) Form: Executory Subordination Provision in Purchase Agreement

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§9.77-9.82.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

9.78-1 Executory subordination provision in purchase agreement

[*Precede with form 9.45-1 or 9.46-1*]

4. Seller agrees to subordinate the lien of the deed of trust described in paragraph 3, above _ _[*one time/from time to time*]**_ _ to the liens of one _ _**[*or more*]**_ _ subsequent deed(s) of trust in accordance with the terms, covenants, and conditions set forth below. Buyer and Seller shall execute a subordination addendum in the form attached as Exhibit _ _**[*see §§9.80-9.82 for Subordination Addendum*]**_ _ to be attached to the deed of trust described in paragraph 3. Seller's obligation to subordinate to subsequent deed(s) of trust securing loan(s) obtained by Buyer (the Subordinating Loans) is subject to the following terms and conditions:**

(a) The proceeds of the Subordinating Loans shall be used only to _ _[*specify, e.g., construct improvements, pay or reimburse Buyer, reimburse trustor for construction or development costs, repay other liens that are senior to Seller's deed of trust*]**_ _;**

(b) The total amount of the Subordinating Loans shall not exceed _ _[*specify dollar amount or percentage of appraised value and describe appraiser's qualifications and procedure for obtaining appraisal*]**_ _;**

(c) The Subordinating Loans shall have the following additional terms and conditions:

(1) The interest rate shall not exceed _ _[*specify fixed percentage or floating index, e.g., the prime rate charged by _ _*[*name*]**_ _** *Bank plus _ _ percent*]**_ _, exclusive of late charges, penalties, or fees payable in case of default;**

(2) The Subordinating Loans shall require _ _[*specify frequency, e.g., monthly*]**_ _ payments of _ _**[*specify, e.g., interest only, amortizing principal and interest payments*]**_ _;**

(3) The Subordinating Loans shall have a term of not less than _ _[*number*]**_ _ _ _**[*months/years*]**_ _ or more than _ _**[*number*]**_ _ _ _**[*months/years*]**_ _;**

(4) The maximum loan fees payable on the Subordinating Loans shall not exceed _ _[*dollar amount*]**_ _; and**

(5) _ _[*Specify other material terms such as prepayment rights or penalties, amount of interest reserve, etc.*]**_ _**

Comment: This provision is to be included in the purchase and sale agreement. It should specify the terms of the subordinating loans in as much detail as possible to protect the seller and to enable the buyer to enforce it if necessary. If the subordinating lien will secure a construction loan, the improvements to be constructed should be described in as much detail as possible. The seller may wish to reduce the risk further by imposing additional conditions on subordination to a construction loan. These conditions will depend on the circumstances of the transaction, but they might include the following requirements:

- The buyer must obtain a firm commitment for a permanent loan;
- The buyer must enter into a satisfactory commercial lease with major tenants for a specified number of square feet of building improvements;
- The buyer must obtain bonding for off-site improvements; or
- The construction lender must agree that (1) the seller will be provided with notice and an opportunity to cure defaults and (2) noncurable defaults will not be grounds for foreclosure if the seller promptly performs all other provisions of the subordinating note and deed of trust.

© The Regents of the University of California

(5) Subordination Addendum

§9.79 (a) Information to Include in Subordination Addendum

The form in §9.80 contains the basic information that should be included in the subordination addendum, which should be attached to and recorded with the seller's deed of trust. The subordination addendum should also address the mechanism for accomplishing the subordination. At a minimum, the addendum should provide for the buyer to notify the seller in writing when a subordination is necessary. The addendum should specify the documents to be given to the seller in connection with the request for subordination and should specify which party is to bear the costs of subordination. The addendum should contain a covenant to execute a standard title company subordination agreement within a given time period and any and all further documents reasonably necessary to effect the subordination. In some circumstances, a buyer may seek a power of attorney to execute the subordination documents on the seller's behalf. The attorney for the seller should recommend against granting a power of attorney so that the seller will retain control over the subordination. The addendum should also specify that it is part of the seller's deed of trust.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.80 (b) Form: Subordination Addendum

§9.80 (b) Form: Subordination Addendum

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§9.77-9.82.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

9.80-1 Subordination addendum

This Subordination Addendum is attached to and forms a part of that certain deed of trust (the Deed of Trust) dated _ _[*date*]_ _, executed by _ _[*name*]_ _ as the trustor in favor of _ _[*name*]_ _ as a beneficiary and naming _ _[*name*]_ _ as the trustee.

In consideration of the trustor's execution and delivery of the Deed of Trust, as long as the trustor is not in default, the beneficiary hereby agrees to subordinate the lien of the Deed of Trust _ _[*one time/from time to time*]_ _ to the lien(s) of one _ _[*or more*]_ _ subsequent deed(s) of trust

[*Add one of the following alternatives*]

[*Alternative 1: If land to be subdivided; individual or blanket loans*]

encumbering any lot or group or groups of lots into which the described property then has been subdivided as shown on a map filed for record, the total number of lots not to exceed _ _[*number*]_ _,

[*Alternative 2: If land already subdivided; individual or blanket loans*]

covering any lot or group or groups of lots described in this agreement,

[*Alternative 3: If land to be subdivided; individual loans only*]

one on each of the lots into which the property will have then been subdivided, as shown on a map filed for record, the total number of lots not to exceed _ _[*number*]_ _,

[*Alternative 4: If improved lot or building site*]

covering the described property,

[*Continue*]

in accordance with the terms, covenants, and conditions set forth in this addendum. Any subordination under this addendum shall be effected through the following procedure:

(a) The trustor shall request the subordination in writing. The written request shall be delivered to the beneficiary together with a sample of the proposed promissory note, deed of trust, assignment of rents, and construction loan agreement for the subordinating loan, the proposed subordination agreement, and other loan documents or information as the beneficiary may reasonably request. The request and loan documents shall specify the lender's identity; the purpose for which borrowed funds may be used; the loan amount, interest rate, and maturity date; and _ _[*specify any other items defined in the subordination agreement; see §§9.76-9.77*]_ _.

(b) The beneficiary shall be entitled to review and approve the loan documents, as long as the beneficiary's approval is not unreasonably withheld or delayed. The beneficiary's approval shall in no event be withheld or delayed if the loan documents contain only the provisions described in this addendum and such other provisions as institutional lenders customarily require for construction loans of the type described in this addendum.

(c) Within _ _[*number*]_ _ days after receipt of the trustor's written request for subordination and the materials provided for above, the beneficiary shall either

(1) deliver to the escrow holder an original subordination agreement duly executed and acknowledged by the beneficiary (in form and substance satisfactory to the beneficiary in the standard form prepared by _ _[*name*]_ _ Title Company) or

(2) deliver to the escrow holder and to the trustor written notice of the beneficiary's specific reasons for not approving the proposed loan and subordination documents.

(d) All subordination costs shall be borne by the _ _[*trustor/beneficiary*]_ _.

(e) The loan shall be evidenced by a promissory note not in excess of

[*Add one of the following alternatives*]

[*Alternative 1: If land to be subdivided or already subdivided; individual or blanket loans*]

an amount arrived at by multiplying the number of lots described in the deed of trust securing the note by _ _[_ _[*dollar amount*]_ _/_ _ *percent of the property's value as appraised by* _ _[*specify identity or qualifications of appraiser*]_ _]_ _.

[*Alternative 2: If land to be subdivided; individual loans only*]

_ _[_ _[*dollar amount*]_ _/_ _ *percent of the appraised value*]_ _.

[*Alternative 3: If improved lot or building site*]

_ _[_ _[*dollar amount*]_ _/_ _ *percent of the property's value as appraised by* _ _[*specify identity or qualifications of appraiser*]_ _]_ _.

[*Continue*]

(f) The loan shall be used for _ _[*specify*]_ _. The loan proceeds shall be disbursed in payment, or in reimbursement for payment, of only the following:

[*Specify uses permitted; see Comment below*]

(g) The subordinating loan documents shall authorize the trustor to receive loan disbursements from the lender by a voucher payment plan based on inspection for work completed and submission by the trustor of an invoice or a voucher for payment of, or for reimbursement for payment of, and release of the lien in connection with the items designated in paragraph _ _[*e.g., (f)*]_ _. The beneficiary's lien priority shall not be reduced as a result of the trustor's misuse of disbursements or the falsity of vouchers or invoices certified and lien releases submitted by the trustor.

Comment: The forms in §§9.81-9.82 provide additional provisions that should, depending on the circumstances, be included in a recorded executory subordination agreement. As recommended above, the agreement should be structured as an addendum to the seller's deed of trust. It may also be necessary to insert certain cautionary language in 10-point or 8-point boldface type at the beginning of the document. See §§9.89-9.94.

The subordination agreement should state clearly what payments may properly be made from the subordinating loan. Disbursements that do not enhance the value of the property increase the encumbrance to which the seller is subordinated without increasing the seller's security. Because this use of funds is unfair to the seller, such an agreement cannot be specifically enforced. *Handy v Gordon* (1967) 65 C2d 578, 55 CR 769. The statement of permitted disbursements in the recorded security instrument is constructive notice to later encumbrancers. The lender's priority under an automatic subordination clause in a deed of trust will require the loan's provisions to meet the conditions under which the seller agreed to subordinate. *Middlebrook-Anderson Co. v Southwest Sav. & Loan Ass'n* (1971) 18 CA3d 1023, 96 CR 338. However, see *Swiss Prop. Mgmt. Co. v Southern Cal. IBEW-NECA Pension Plan* (1997) 60 CA4th 839, 70 CR2d 587, in which riders to deeds of trust that required a lender to disburse loans only for construction purposes were superseded by a CLTA form subordination agreement. See §9.84. For this reason, the seller may be required to execute an additional subordination agreement specifically describing the subordinating loan. See §9.82.

PRACTICE TIP: Institutional lenders require title insurance insuring the priority of their deed of trust. If the lender's

priority is to be insured, the agreement must provide that its lien will retain priority under terms acceptable to the lender. These are matters for negotiation among the buyer, seller, and lender. On endorsements available for lenders regarding subordinations, see California Title Insurance Practice §§8.95-8.96 (2d ed Cal CEB 1997).

This form should be used to ensure that proper controls are retained for disbursements under the senior construction loan. The suggested provision calls for the voucher system frequently adopted by lenders and retains the lender's lien priority when that system is used. The voucher system is discussed in California Mechanics' Liens and Related Construction Remedies §§8.48, 8.75 (3d ed Cal CEB 1998). A developer who is unaccustomed to working under a voucher system might refuse to accept this provision. In that case, the seller might consider requiring that the buyer furnish a surety bond under which the seller would be an obligee. Opinions differ about the efficacy of a bond in this situation. The method used and the extent to which each party's interests will be protected are matters for negotiation. Other methods include requiring the seller's approval and execution of voucher requests, and employing an independent third party (such as Builders Control Escrow) to disburse the construction loan proceeds.

Whatever method is used, the buyer will incur additional costs in the form of loan fees, insurance premiums, and other charges. These costs may be accounted for in the subordination agreement by fixing a maximum for them and allowing them to be paid from the proceeds of the construction loan.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.81 (c) Form: Subordination to Permanent Loan

§9.81 (c) Form: Subordination to Permanent Loan

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§9.77-9.82.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

9.81-1 Subordination to permanent loan

[*Precede with form 9.80-1*]

After completion of the construction of improvements on the property as described in paragraph _ _[*number*]**_ _, the Deed of Trust shall be subordinated to a deed of trust securing a permanent loan on _ _**[*the property/the lot/each lot*]**_ _ from a bank, a savings and loan association, or an insurance company (or other institutional lender), as long as the total amount of indebtedness secured by liens on the property that are senior to this Deed of Trust do not exceed _ _[_ _**[*dollar amount*]**_ _/_ _ *percent of the appraised value*]**_ _, including all costs of obtaining the loan or discounts not in excess of _ _**[*dollar amount*]**_ _, and containing the following additional terms: _ _**[*Specify interest rate, term, etc.; see form 9.78-1*]**_ _.**

Comment: The construction loan is frequently based on a commitment for a permanent loan after construction is completed, and the seller will want assurance that a commitment for permanent financing has been obtained. See §9.76. If the seller intends to retain the deed of trust after the permanent financing is obtained, the subordination agreement should provide for further subordination to the permanent loan, requiring that the permanent loan be used to pay the construction loan in full. Often, the seller will require that the note be paid when the construction loan matures, especially if the amount of the permanent loan will exceed the amount necessary to pay off the construction loan. The same need for certainty about lender, maximum amount, interest rate, maturity date, and amortization applies for permanent loans as for construction loans. See §9.75.

With developments built for resale, subordination to a permanent loan should permit payment to the seller when the property is sold to the ultimate purchaser. This result might be accomplished by either

- accelerating the buyer's note on resale to the extent of the release price per lot (see §§9.100-9.110 on release clauses); or
- leaving this aspect of subordination to future negotiations and omitting the provision from the purchase and sale agreement or subordination addendum. If this issue is left to future negotiations, any new agreement must be supported by new consideration. CC §1698.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.82 (d) Form: Execution of Additional Subordination Agreement

§9.82 (d) Form: Execution of Additional Subordination Agreement

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§9.77-9.82.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

9.82-1 Execution of additional subordination agreement

[*Precede with form 9.80-1*]

Seller agrees, on request, to execute and deliver to Buyer for recordation a subordination agreement or agreements in the form attached as Exhibit _ _, in favor of any lender's loan to which Seller's lien is to be subordinated under the terms of this Deed of Trust. The terms of any such subordination agreement executed by Seller shall prevail over the subordination terms provided for in this Deed of Trust.

Comment: Title companies generally require that a specific subordination agreement be executed by the seller and recorded concurrently with the subordinating loan. See §9.80. The form of the subordination agreement to be attached must be acceptable to the title company insuring the subordinating loan. See *Swiss Prop. Mgmt. Co. v Southern Cal. IBEW-NECA Pension Plan* (1997) 60 CA4th 839, 70 CR2d 587. Subordination agreements satisfactory to title companies have been prepared by the California Land Title Association and are available from most title companies. Any variation from these forms should be approved in advance by the title company that will insure the priority of the subordinating loan. In addition, using a title company's proprietary form leaves the title company with less room to dispute coverage if priority issues arise out of a challenge to the adequacy of the form.

The clause above is an expansion of the requirement in form 9.80-1 at (c)(1).

© The Regents of the University of California

§9.83 b. Executed Subordination Agreement

There are two types of executed subordination agreements: an agreement that was previously executory and an automatic subordination agreement. An automatic subordination occurs when the seller's lien is recorded together with an executed agreement that provides that the lien of the subsequent construction or take-out loan will automatically be senior to the seller's lien. *Carpenson v Najarian* (1967) 254 CA2d 856, 62 CR 687; *Joanaco Projects, Inc. v Nixon & Tierney Constr. Co.* (1967) 248 CA2d 821, 57 CR 48. To insure the lien of the later, subordinating deed of trust as senior to the subordinated deed of trust, title companies usually require execution of an additional agreement subordinating the seller's lien to the particular construction loan obtained. 5 Miller & Starr, California Real Estate §11:187 (3d ed 2000). For this reason, automatic subordination is particularly disfavored or is combined with an obligation to execute a formal subordination agreement at the time the subordinating lien is recorded. If there is any variation between the new agreement and the original subordination agreements, the new agreement will be unenforceable unless it is supported by new consideration. *Miller v Citizens Sav. & Loan Ass'n* (1967) 248 CA2d 655, 56 CR 844. For further discussion of automatic subordination and form, see §§9.86-9.87.

When a subordinating loan is made in reliance on an automatic subordination agreement, or when a subordination is made under a previously executory agreement, the legal problems that may arise will differ from those encountered in executory agreements (see §§9.75-9.78). If the new loan complies precisely with the subordination agreement, and if the funds are not misapplied, an agreement that when still executory might have been too uncertain to be enforceable becomes a valid executed agreement, and the new loan achieves priority over the seller's lien. If, however, the new loan does not conform with the subordination agreement, either because of a discrepancy in the loan terms or because loan funds are misapplied, the new lender may not be able to attain the priority sought despite the subordination agreement.

© The Regents of the University of California

§9.84 (1) Discrepancy Between Agreement and Loan

A discrepancy between the loan described in the subordination agreement and that actually entered into may entitle the seller's deed of trust to retain priority. A change in the interest rate or term, or inclusion of other clauses adversely affecting the seller's interests, might be sufficient to invalidate the subordination. In *Collins v Home Sav. & Loan Ass'n* (1962) 205 CA2d 86, 22 CR 817, the interest rate charged complied with the subordination agreement, but a 13.5-percent loan placement fee did not, and the seller's lien retained its priority.

© The Regents of the University of California

§9.85 (2) Misapplication of Funds

If the construction lender knows or should know of the buyer's application of loan funds to uses or purposes not permitted by the subordination agreement, the construction lien may lose its priority. *United States Bldg. & Loan Ass'n v Salisbury* (1932) 217 C 35, 17 P2d 140; *Radunich v Basso* (1965) 235 CA2d 826, 45 CR 824. In one decision, the court allowed the construction lender priority to the extent that funds were disbursed in accordance with the subordination agreement but held that the lender's lien was junior to the seller's lien to the extent that funds were misapplied. *Miller v Citizens Sav. & Loan Ass'n* (1967) 248 CA2d 655, 56 CR 844. Note that this holding created three encumbrances rather than two: a lien for the amount of the properly used funds, the seller's subordinated lien, and the lien for the misapplied funds.

Some buyers have attempted to avoid this rule by including in the subordination agreement a conclusive presumption that the construction loan funds have been properly applied. In *Joanaco Projects, Inc. v Nixon & Tierney Constr. Co.* (1967) 248 CA2d 821, 57 CR 48, the court held such a purported presumption ineffective to shelter the buyer from immunity for its own misconduct.

Sellers have had less success in recovering damages for lenders' misfeasance in failing to ensure the buyers' compliance with the subordination agreement than in retaining the priority of the sellers' liens, as in the cases cited above. Courts have held that the lender owes no duty of care to the seller, because there is no privity of contract between lender and seller. *Weiss v Brentwood Sav. & Loan Ass'n* (1970) 4 CA3d 738, 84 CR 736; *Fries v Broadway Fed. Sav. & Loan Ass'n* (1968) 258 CA2d 119, 65 CR 460; *Gill v Mission Sav. & Loan Ass'n* (1965) 236 CA2d 753, 46 CR 456; *Matthews v Hinton* (1965) 234 CA2d 736, 44 CR 692.

© The Regents of the University of California

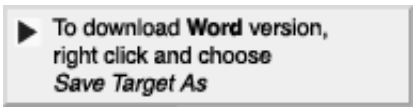
§9.86 (3) Automatic Subordination Agreement

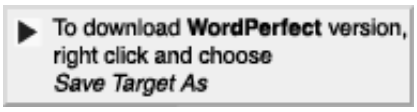
An automatic subordination clause differs from the executory subordination agreement only in the way the subordination becomes effective. In other words, the automatic subordination agreement provides that the deed of trust is subordinated when the later deed of trust meeting the terms of the clause is recorded. The subordination agreement in §§9.80-9.82 contemplates that additional acts will be necessary to effect the subordination.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.87 (4) Form: Automatic Subordination Agreement

§9.87 (4) Form: Automatic Subordination Agreement





9.87-1 Automatic subordination agreement

As long as no unrescinded notice of default under its terms then appears of record, this Deed of Trust shall be subordinate to deed(s) of trust thereafter executed by the trustor

[*Continue by specifying terms of subordinating loan; see forms in §§9.80-9.82*]

Comment: This clause is used together with the specific description of the loan terms, as in form 9.80-1. It provides for automatic subordination if no default appears of record. The seller may prefer permitting subordination only if no default exists under the deed of trust. For similar language on reconveyance, see §9.105. Title companies will almost universally not insure the priority of the subordinating loan based on an automatic subordination clause. Instead, a subordination agreement executed by the seller expressly subordinating the purchase money deed of trust to the new loan must usually be recorded concurrently with the new loan instruments. See §9.82. Thus, little reliance should be placed on an automatic subordination clause, and a formal subordination agreement should be executed concurrently with the recordation of the subordinating lien.

© The Regents of the University of California

§9.88 c. De Facto Subordination Agreement

A de facto subordination is created when the seller and the buyer agree that, at close of escrow, the construction deed of trust will be recorded first and the purchase money deed of trust recorded second and subordinated to the construction lender's lien. Some commentators contend that such an agreement does not result in reordering the priority of the liens and is thus not a true subordination situation. See 5 Miller & Starr, California Real Estate §§11:193-11:195 (3d ed 2000). For all practical purposes, however, courts have treated this situation as raising the same issues that exist under subordination agreements (see §§9.75-9.76), regardless of the mechanics used. Thus, whether the lender's lien retains priority still depends on whether the construction loan complies with the conditions under which the seller agreed to modify the order of recording (*Middlebrook-Anderson Co. v Southwest Sav. & Loan Ass'n* (1971) 18 CA3d 1023, 96 CR 338), and the construction lender faces the same risk of loss of priority when funds are misused as under any other form of subordination (*Gluskin v Atlantic Sav. & Loan Ass'n* (1973) 32 CA3d 307, 108 CR 318).

The case of *Friery v Sutter Buttes Sav. Bank* (1998) 61 CA4th 869, 72 CR2d 32, restricted *Gluskin v Atlantic Sav. & Loan Ass'n, supra,* to situations in which a seller, having taken back a lien on the property, subordinated its position to the buyer's lender. However, when the seller voluntarily acquires a position junior to a *preexisting* lienholder, absent special circumstances the senior lienholder owes the junior no duty to refrain from modifying the senior indebtedness that would substantially impair the junior note or increase the likelihood of default. 61 CA4th at 871.

The lender must also comply with subordination conditions of which it has actual or constructive knowledge. *Plastino v Eureka Fed. Sav. & Loan Ass'n (In re Sunset Bay Assocs.)* (9th Cir 1991) 944 F2d 1503.

© The Regents of the University of California

§9.89 3. Cautionary Language Required

The Civil Code requires that specific warnings be given in subordination provisions to advise the holder of the lien being made junior of that fact and its implications. Warnings must be included in certain instruments containing subordination clauses (CC §2953.2) and subordination agreements (CC §2953.3), but they need not appear in a purchase agreement that provides for the seller to carry back a second deed of trust. The statutes do not apply when the subordination provisions expressly state that the subordinating loan is to exceed $25,000 (CC §2953.5(a)) or when the subordinated loan exceeds $25,000 (CC §2953.5(b)). Although these statutes thus apply to very few real property transactions, many title companies insist that the statutory language be inserted in any deed of trust with subordination provisions.

© The Regents of the University of California

§9.90 a. Automatic Subordination

If, under the terms of the instrument creating it, a security interest becomes subordinate to another lien when certain conditions occur, the instrument containing the subordination provision must have the word "subordinated" at its top in at least 10-point bold type if printed or in capital letters and underlined if typewritten. CC §2953.2. The following provision must appear immediately below in at least 8-point bold type if printed or in capital letters if typewritten (CC §2953.2(b)):

NOTICE: This _ _[*insert description of real property security instrument*]**_ _ contains a subordination clause which may result in your security interest in the property becoming subject to and of lower priority than the lien of some other or later security instrument.**

© The Regents of the University of California

§9.91 b. Security Instrument Permits Proceeds to be Used for Nonimprovement Purposes

If the security instrument permits the proceeds of the new senior loan to be used for purposes other than paying for improvement of the land, CC §2953.2 requires that the following provision appear immediately above the space for the signature of the subordinated lienor in at least 8-point bold type if printed or in capital letters if typewritten (CC §2953.2(c)):

NOTICE: This _ _[*insert description of real property security instrument*]**_ _ contains a subordination clause that allows the person obligated on your real property security instrument to obtain a loan a portion of which may be expended for other purposes than improvement of the land.**

For situations in which the lender's subordinating lien achieves priority by being recorded earlier than the seller's subordinated lien, the California Attorney General has declared that the notice provisions of CC §2953.2 do not apply. 43 Ops Cal Atty Gen 19, 22 (1964). If the subordinating or subordinated lien is less than $25,000, however, the statutory notice must be included in deeds of trust on subordination agreements if the forms in §§9.78, 9.80-9.82 are used.

© The Regents of the University of California

§9.92 c. Agreement Causes Security Interest to Become Junior

An agreement that causes a security interest to become junior to a new loan, either conditionally or otherwise, must have the words "subordination agreement" at the top in at least 10-point bold type if printed or in underlined capital letters if typewritten. CC §2953.3. The following language must appear immediately below in at least 8-point bold type if printed or in capital letters if typewritten (CC §2953.3(b)):

NOTICE: This subordination agreement _ _[*may result/will result*]**_ _ in your security interest in the property becoming subject to and of lower priority than the lien of some other or later security instrument.**

© The Regents of the University of California

§9.93 d. Agreement Permits Proceeds to be Used for Nonimprovement Purposes

If the agreement permits the proceeds of the new senior loan to be used for purposes other than actual contract costs for improving the property, the following statement must appear immediately above the space for the signature of the subordinated lienor in at least 8-point bold type if printed or in capital letters if typewritten (CC §2953.3(c)):

NOTICE: This subordination agreement contains a provision that _ _[*allows/may allow*]_ _ the person obligated on your real property security to obtain a loan a portion of which may be expended for other purposes than improvement of the land.

© The Regents of the University of California

§9.94 e. Right to Waive

These statutory provisions may be waived by the person whose lien is being subordinated. CC §2953.4(c). However, because the Attorney General has declared that the subordinated lien must be signed and delivered before any steps are taken to sign the waiver (43 Ops Cal Atty Gen 19 (1964)), including the statutory language is preferable to relying on the seller's willingness to waive his or her rights after the event.

© The Regents of the University of California

4. Effect of Subordination on Antideficiency Rules

§9.95 a. Exemption From Antideficiency Protection

A buyer who executes a note and deed of trust in favor of the seller receives the antideficiency protection of CCP §580b. However, the later subordination of the seller's deed of trust may entitle the seller to recover a deficiency judgment despite §580b.

When the seller agrees to an actual subordination of the purchase money deed of trust to a construction loan, the purchase money antideficiency protection of CCP §580b no longer applies. The change in use of the property renders the present security value of the property irrelevant. *Spangler v Memel* (1972) 7 C3d 603, 102 CR 807. The supreme court reasoned in *Spangler* that the intended purpose of §580b—to place the risk of overvaluation on the seller—would not be furthered by applying it in this situation. The purpose of §580b is not served by having the subordinating seller bear the risk of the ultimate success of the construction project. Thus, a sold-out-seller junior lienholder whose deed of trust is subordinated to construction financing may sue on the promissory note representing the unpaid balance of the purchase price.

© The Regents of the University of California

§9.96 b. Express Waiver Not Required

The buyer in *Spangler v Memel* (1972) 7 C3d 603, 102 CR 807 (see §9.95) had specifically agreed to waive CCP §580b and personally guaranteed the seller's carryback note. However, a subordinating seller appears to benefit from the *Spangler* court's ruling even without this explicit waiver. In *Jack Erickson & Assocs. v Hesselgesser* (1996) 50 CA4th 182, 57 CR2d 591, the court held that the buyer waived §580b protection by having the seller subordinate his security to a construction loan and by later inducing the seller to reconvey the deed of trust so that the buyer could complete a sale to a third party. In *Ziegler v Barnes* (1988) 200 CA3d 224, 246 CR 69, and *Boyle v Sweeney* (1989) 207 CA3d 998, 255 CR 153, subordinating sellers were not barred from recovery by §580b even though no written agreement waiving §580b was executed by the buyer.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.97 c. Mere Promise to Subordinate Not Sufficient

§9.97 c. Mere Promise to Subordinate Not Sufficient

The antideficiency exception specified in *Spangler v Memel* (1972) 7 C3d 603, 102 CR 807 (see §§9.95-9.96) will not apply if the lender agrees to subordinate to future improvement loans, but fails in fact to subordinate. *Crookall v Davis, Punelli, Keathley & Willard* (1998) 65 CA4th 1048, 77 CR2d 250.

Moreover, the courts have questioned the validity of a contractual waiver of CCP §580b that does not involve actual subordination of the loan, as contrasted with an agreement to subordinate, which is not implemented. See *DeBerard Props. v Lim* (1999) 20 C4th 659, 85 CR2d 292; *Webber v Inland Empire Invs., Inc.* (1999) 74 CA4th 884, 88 CR2d 594; *Budget Realty, Inc. v Hunter* (1984) 157 CA3d 511, 204 CR 48.

© The Regents of the University of California

§9.98 d. Nonconstruction Loan

The cases following *Spangler v Memel* (1972) 7 C3d 603, 102 CR 807, all arose when the seller's lien was subordinated to a construction deed of trust. The *Spangler* rationale does not defeat the buyer's protections under CCP §580b when the seller subordinates to a loan that is *not* a construction loan (as when, *e.g.,* a buyer desires to refinance a first loan that was taken subject to or assumed). In *Thompson v Allert* (1991) 233 CA3d 1462, 285 CR 367, the court specifically stated that the *Spangler* rationale is limited to situations in which the seller's loan is subordinated to another loan, such as a construction loan, that signals a profound change in the use to which the property is devoted. Further, a mere agreement to subordinate will not defeat §580b if no subordination occurs.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.99 e. Relevance of Loan Amount

§9.99 e. Relevance of Loan Amount

Code of Civil Procedure §580b does not to apply if the amount of the construction loan is significantly disproportionate to the property's value at the time of sale, resulting in a "pronounced intensification" in the postsale use of the property. See *Lawler v Jacobs* (2000) 83 CA4th 723, 735, 100 CR2d 52.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.100 B. Release and Partial Reconveyance

§9.100 B. Release and Partial Reconveyance

A buyer who intends to develop real property in increments, or to subdivide and sell the lots separately, may need to release portions of the real property from the lien either when the construction loan is recorded for each phase of the development (in the absence of a subordination agreement) or when the subdivided lots are sold. Subordination agreements are discussed in §§9.66-9.99. The proceeds from the construction loan or sale will normally provide the consideration for partial releases.

At the time the purchase and sale agreement is executed, a developer may not have sufficient information to know exactly how the property will be improved. Many factors, including financing, governmental requirements, the cost and method of providing utilities and road access, soil conditions and drainage, and market demand will affect the type, design, and schedule of development. Therefore, specific legal descriptions of the parcels or lots to be partially released may not be available when the purchase agreement or option is prepared, and the buyer will need a release clause with a great deal of flexibility in selecting what parcels are to be released, and in what order.

The seller must be assured that the security for the deed of trust will not be impaired by releases made to the buyer. To protect the seller, restrictions must be placed on the buyer's release of parcels to ensure that the value of the property remaining subject to the seller's lien after each release will be adequate security for the balance of the seller's purchase money note. One device for achieving this protection is to require that releases be made in a stated order, with the less valuable first. Another method is to fix the release price higher than the prorata portion of the purchase price allocable to the released parcel.

A purchase and sale agreement allowing for partial releases without adequate protection for the seller will be unenforceable because the agreement either lacks the necessary certainty (*White Point Co. v Herrington* (1968) 268 CA2d 458, 73 CR 885) or is unfair to the seller (*Eldridge v Burns* (1982) 136 CA3d 907, 186 CR 784). The requirements of certainty and fairness are discussed in §§9.101-9.102. The seller may also use release provisions to discourage delinquency by conditioning the right to a release on the absence of a default or of a recorded notice of default. These protections are provided in forms 9.105-1—9.106-1.

PRACTICE TIP: Counsel for buyer and seller must often reconcile the buyer's need for flexibility in releasing parcels with the seller's need for certainty and fairness to protect his or her security and to ensure the legal enforceability of the agreement. Resolving these competing needs calls for skilled negotiating and careful drafting. Usually, the buyer's and the seller's requirements are met by giving the buyer some discretion to define the boundaries of the release parcels, but limiting this discretion to ensure that its exercise will not impair the seller's security. A form limiting the buyer's discretion to set the boundaries of release parcels is in §9.106; an alternative form, protecting the seller's security by adjusting release prices, is in §9.107.

The buyer and the seller can agree that portions of the property will be released from the lien of the deed of trust on the entire property on payment of specified consideration. The release is accomplished by a partial reconveyance, executed by the trustee, that describes the released portion. Civil Code §2941 requires reconveyance on full satisfaction of the indebtedness, but there are no statutes requiring partial reconveyance or release on partial payment. Without an enforceable agreement between the trustor and the beneficiary, the trustor is not entitled to a partial release in exchange for partial satisfaction. See CC §2912; *Bradbury v Thomas* (1933) 135 CA 435, 27 P2d 402. A trustee who wrongfully releases and reconveys is liable in damages to the beneficiary. *Doyle v Surety Title & Guar. Co.* (1968) 261 CA2d 525, 68 CR 177.

PRACTICE TIP: The preferred practice is to include release clauses in both the purchase and sale agreement and the purchase money deed of trust, although a separately recorded release agreement is enforceable (*Woodward v Brown* (1897) 119 C 283, 51 P 542). The property to be released may be described by lot, by metes and bounds, or by any other means that is sufficiently specific. See §§9.101-9.102. Compliance with the Subdivision Map Act is required at all times to ensure legality of the lot release. Govt C §§66410-66499.37. See §9.103.

Effective January 1, 2001, amendments to CC §2941 set a deadline within which a secured party must act to release its lien, and limit a secured party's ability to charge a fee in connection with filing the release. That section further requires that a request for reconveyance be executed and delivered within 30 calendar days after (1) a mortgage has been satisfied, or (2) the obligation secured by a deed of trust has been satisfied. It also requires that the secured party deliver the original note marked "paid in full" to the trustee or borrower. Further, the amendments prohibit recovery of any fee not expressly provided for in the statute.

Title companies customarily handle the mechanics of partial releases and reconveyances, and their guidance in any given instance may be very useful. On endorsements available for partial reconveyances, see California Title Insurance Practice §§8.91-8.92 (2d ed Cal CEB 1997).

© The Regents of the University of California

1. Requirement of Certainty and Fairness

§9.101 a. Impact on Specific Performance

To be enforceable by the buyer, a release clause must be both certain and fair to the seller. If the transaction itself is still executory, an uncertain release clause will deny the buyer specific performance of the entire purchase agreement. If the sale has been consummated and only the release provisions remain executory, the seller cannot rescind the conveyance but the buyer will be denied specific performance of the release clause.

In *White Point Co. v Herrington* (1968) 268 CA2d 458, 73 CR 885, the entire sale was still executory, and the escrow instructions provided that the note would contain a release clause for partial releases at $3000 per acre. The court held this provision to be uncertain and denied the buyer specific performance of the entire agreement, stating that, when only the broadest guidelines for releases are given, the contract is unfair to the seller because of the possibility that the best parcels could be released, leaving the seller with land of less value than the balance due on the note.

In *Lawrence v Shutt* (1969) 269 CA2d 749, 75 CR 533, the buyer sued for specific performance of the release clause after the property had been conveyed, and the seller cross-complained for rescission of the entire transaction. Although the release clause was quite detailed, the court found it uncertain because it provided that each parcel to be released had to be contiguous to the portion previously released, without specifying the precise area to be released. Although the uncertainty of the release clause precluded specific performance, it was not a reason to invalidate the otherwise complete conveyance, and the seller was denied rescission.

The decisions in both *White Point Co. v Herrington, supra,* and *Lawrence v Shutt, supra,* relied on *Handy v Gordon* (1967) 65 C2d 578, 55 CR 769, a case concerning subordination (see §9.75), for the proposition that enforcement of subordination and release clauses requires certainty and fairness to the seller. The underlying rationale of all three cases seems to be that a seller is not adequately protected unless the subordination and release clauses are sufficiently certain to ensure that the seller's security is not impaired. The test contains an element of subjectivity, which calls for extremely careful drafting to make release clauses enforceable.

© The Regents of the University of California

§9.102 b. Impact on Damages

When a seller has accepted substantial payments on an obligation secured by a deed of trust that permits partial releases for such payments, the buyer may be entitled to equitable relief or damages even though the buyer may not otherwise be entitled to enforce the release provisions because of their uncertainty or unfairness. *Eldridge v Burns* (1982) 136 CA3d 907, 186 CR 784. The trial court in *Eldridge* rescinded the sales contract, retroactive to the date of the buyer's original demand for release under the release clause, and awarded the buyer restitution of the principal paid less the taxes, assessments, accrued interest, and legal expenses the seller incurred in evicting tenants from the property. The seller was not allowed any offset for the 3 years of the buyer's possession after the original demand for release.

An uncertain release clause in a purchase agreement will thwart a buyer's demand for specific performance; furthermore, its unfairness is not a defense in an action by the seller for damages for breach of the purchase agreement. *Yackey v Pacifica Dev. Co.* (1979) 99 CA3d 776, 160 CR 430. The release clause in *Yackey* was similar to that in *White Point Co. v Herrington* (1968) 268 CA2d 458, 73 CR 885, but its uncertainty, which the buyer could abuse by selecting the best parcels for release, could not be used defensively by the buyer, who had drafted it.

© The Regents of the University of California

2. Subdivision Requirements

§9.103 a. Subdivision Map Act

If the property to be sold is currently undivided, partial releases will probably constitute division of the property, requiring compliance with the Subdivision Map Act (Govt C §§66410-66499.37). The release clause should provide that the buyer's entitlement to a partial release is conditioned on compliance with the Act. See form 9.106-1.

Under the Subdivision Map Act, local jurisdictions must adopt ordinances regulating and controlling subdivisions and providing for recording of an approved map when land is divided (see §§1.73-1.90). Govt C §§66411-66411.1; see *Friends of Lake Arrowhead v Board of Supervisors* (1974) 38 CA3d 497, 113 CR 539. The Act is intended to encourage orderly community development by providing for control of the design and improvement of subdivisions (*Newport Bldg. Corp. v City of Santa Ana* (1962) 210 CA2d 771, 26 CR 797; 56 Ops Cal Atty Gen 496 (1973)) and to permit the imposition of conditions on subdivision approval to prevent the subdivision from becoming an undue burden on the community's taxpayers (*Bright v Board of Supervisors* (1977) 66 CA3d 191, 135 CR 758).

An approved subdivision map must be recorded for any subdivision as defined in the Act. Subdivision is defined as the division of improved or unimproved land shown on the latest county assessment roll as a unit or contiguous units, for the purpose of sale, lease, or financing, whether immediate or future. Govt C §66424. Both tentative and final maps must be approved for a subdivision creating five or more parcels unless the subdivision comes within one of the exceptions listed in Govt C §66426. Subdivisions of fewer than five parcels are exempt from §66426 but must obtain a parcel map. Govt C §66428. Procedures for preparing and obtaining approval of tentative, final, and parcel maps are set forth in Govt C §§66433-66463.5. See *Lenny v Board of Supervisors* (1974) 41 CA3d 902, 116 CR 500.

The California Attorney General has interpreted Govt C §66424 to include within its definition of subdivision the placing of two separate deeds of trust on different portions of a single lot or parcel. 58 Ops Cal Atty Gen 408 (1975). The opinion cites legislative history to show that the term "financing" was added to former Bus & P C §11535 (the predecessor to Govt C §66424) to prevent circumvention of the Subdivision Map Act through subdivision by financing. This reasoning would seem to apply to partial releases from a blanket encumbrance of portions of currently undivided land.

See also California Subdivision Map Act and the Development Process (2d ed Cal CEB 2001).

© The Regents of the University of California

§9.104 b. Subdivided Lands Act

Under the Subdivided Lands Act (Bus & P C §§11000-11200), an owner or a subdivider is prohibited from selling a lot or a parcel subject to a blanket encumbrance unless certain conditions are met. Bus & P C §11013.1. The prohibition can be avoided if the blanket encumbrance contains an unconditional release clause. Bus & P C §11013.1. The provisions set forth in §§9.105-9.107 are not unconditional release clauses and thus do not meet the exception of §11013.1. The subdivider can still sell lots subject to a blanket encumbrance by complying with one of three methods for protecting the purchaser's deposit (Bus & P C §11013.2):

- Placing the purchaser's funds in an escrow account;
- Conveying the subdivision property in trust; or
- Posting a bond.

The subdivider would have to meet one of these exceptions to qualify to sell lots under the release clauses in §§9.105-9.107.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.105 3. Form: Partial Release of Determined Lots

§9.105 3. Form: Partial Release of Determined Lots

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§9.105-9.110.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

9.105-1 Partial release of determined lots

[*If appropriate, add to section 3.6 of the purchase and sale agreement (form 4.176-6)*]

The Deed of Trust shall contain the following provisions:

The beneficiary shall cause the trustee to release and execute partial reconveyances of any one or more of the parcels of real property described in the schedule set forth below from the lien of this Deed of Trust on satisfaction of each of the following conditions:

(a) No release will be given if a notice of default then appears of record, or if any condition exists under the Deed of Trust that, with the passage of time, would entitle the beneficiary to record a notice of default.

(b) No portion of the real property will be released unless all other portions of the real property subject to this Deed of Trust identified with a lower number than the number identifying the portion sought to be released have been reconveyed.

(c) No release will be given unless the trustee holds and is authorized to deliver to the beneficiary, concurrently with the partial reconveyance, the release price for the property to be released as set forth in the schedule of release parcels and release prices below.

(d) No release will be given unless the trustee holds and is authorized to deliver to the beneficiary, in addition to the sum computed under (c) above, an amount equal to the accrued interest and any late charges on the promissory note secured by this Deed of Trust through the date of reconveyance.

The portions of the real property described above that are subject to partial release, the price to be paid for the release of each such portion (under (c) above), and the order of release, are as follows:

Schedule of Release Parcels and Release Prices

Property to be released	**Release price**
1. _ _[*Legal description of lot or parcel*]_ _	_ _[*dollar amount*]_ _
2. _ _[*Legal description of lot or parcel*]_ _	_ _[*dollar amount*]_ _

[*Continue as needed*]

Payments for releases under (c) above, except periodic payments required by the note, shall be applied to the _ _[*next/final*]_ _ payment on the note secured by this Deed of Trust. Payments under (d) above shall be applied to accrued interest on the note. Principal payments made on the note for which no releases are obtained by the trustor shall constitute a credit fund to apply against subsequent releases from the lien of this Deed of Trust.

Comment: This form is to be used when the lots to be released have already been identified. Forms 9.106-1 and 9.107-1 suggest two methods of permitting partial release when the agreement is drafted before the property is subdivided.

The release clause must fit the particular features of a given transaction to ensure that any discretion of the buyer

regarding the lots to be released cannot be exercised in a way that might be unfair to the seller. This form provides one method for limiting the buyer's discretion.

The agreement must specify the extent and manner of application of release payments to the contract balance. Lack of clarity or inaccuracy may bring about unintended results. *San Diego Constr. Co. v Mannix* (1917) 175 C 548, 166 P 325; *Vilkin v Sommer* (1968) 260 CA2d 687, 67 CR 837. The buyer usually prefers to have payments apply to the next payment due under the note, and to apply all payments, including the downpayment, to the release price. The seller may prefer to credit payments to the last payment due. The manner of crediting payments must be tailored to fit the needs of the parties to the transaction.

Usually, the buyer does not lose the right to partially reconvey by failing to request the release of land when payments are made. Absent a contrary provision in the agreement, the trustor's subsequent default does not extinguish the right to partial reconveyances of land already paid for. *Eldridge v Burns* (1982) 136 CA3d 907, 186 CR 784; *Conley v Poway Land & Inv. Co.* (1965) 232 CA2d 22, 42 CR 636.

For provisions allowing releases even when the buyer's annual payments are limited, as in form 9.46-1, see form 9.109-1.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.106 4. Form: Partial Release (Lots Not Determined); Limiting Buyer's Discretion

§9.106 4. Form: Partial Release (Lots Not Determined); Limiting Buyer's Discretion

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§9.105-9.110.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

9.106-1 Partial release (lots not determined); limiting buyer's discretion

[*If appropriate, add to section 3.6 of the purchase and sale agreement (form 4.171-6)*]

The Deed of Trust shall contain the following provisions:

The beneficiary shall cause the trustee to release and execute partial reconveyances of portions of the real property described above from the lien of this Deed of Trust on satisfaction of each of the following conditions:

(a) _ _[*Describe order of reconveyance and any other limitations necessary to prevent impairment of the seller's security; see Comment for examples.*]_ _

(b) No release will be given if _ _[*a notice of default then appears of record/the trustor is then in default under this Deed of Trust*]_ _**.**

(c) The trustee holds and is authorized to deliver to the beneficiary the sum of _ _[*dollar amount*]_ _ **for each acre for which release is sought by the trustor.**

(d) The trustee holds and is authorized to deliver concurrently with the partial reconveyance to the beneficiary, in addition to the sum required by (c) above, an amount equal to the accrued interest on the promissory note secured by this Deed of Trust through the date of reconveyance.

(e) Each portion of the real property released from the lien of this Deed of Trust shall consist of one or more legal lots or parcels as shown on a recorded parcel or final map. Despite the description of the release parcels in paragraph (a) above, the trustor reserves the right, in satisfying this condition, to have the beneficiary cause the trustee to release less than the entire portion of the real property that the trustor would otherwise be entitled to have released because of the payment made. Portions of the real property not included in a partial release under this provision, but included in computing the principal payment required to obtain a partial release, shall not be included in computing the principal payment required to obtain any subsequent release that includes that portion, or any part of it.

[*Continue with last paragraph in form 9.105-1*]

Comment: This form gives the buyer credit on releases for payments previously made for which reconveyances were not received. On balancing the needs of the buyer and the seller in drafting release clauses, see §9.100; on the requirements of certainty and fairness, see §§9.101-9.102; for provisions for the release of determined lots, see §9.105.

The order of reconveyance in the agreement (see paragraph (a)) might be stated in a manner such as the following when, *e.g.,* the southerly portion of the property is the most valuable, and the property is approximately square:

The first parcel to be reconveyed shall have as its northerly, westerly, and southerly boundaries the northerly, westerly, and southerly boundaries, respectively of the property, and the easterly boundary shall be parallel to the westerly boundary. Subsequent releases shall each have as a westerly boundary the easterly boundary of the previously released parcel, an easterly boundary parallel to the westerly boundary, and as its northerly and southerly boundaries the northerly and southerly boundaries, respectively, of the property. In no event shall any reconveyance be permitted if the property remaining subject to the lien of this deed of trust would contain fewer than _ _[*number*]_ _ **square feet as a result.**

Another way of providing for the order or reconveyance when, *e.g.,* the property is rectangular in shape with greater depth than frontage and the southerly portion of the property is most valuable, might be:

The first parcel to be reconveyed shall have as its northerly and westerly boundaries the northerly and westerly boundaries of the property; the length of the westerly boundary shall not exceed the length of the northerly boundary of the land released; the southerly and easterly boundaries shall be parallel respectively to the southerly and easterly boundaries of the property. Subsequent releases shall have as a westerly boundary the easterly boundary of the parcel previously released, the northerly, easterly, and southerly boundaries shall be parallel to the northerly, easterly, and southerly boundaries of the property until the easterly boundary of the property is reached and subsequent releases shall be subject to the above conditions as if the southerly boundary of the land then released is the northerly boundary of the property. In no event shall any such release, other than a release having as its easterly boundary the easterly boundary of the property, have its easterly boundary closer than _ _[*number*]_ _ feet from the easterly boundary of the property, as measured at right angles from the easterly boundary. In no event shall any such release, other than a release having as its southerly boundary the southerly boundary of the property, have its southerly boundary closer than _ _[*number*]_ _ feet from the southerly boundary of the property, as measured at right angles.

When frontage or other preferred land is to be released only after the remainder of the property has been released, and, *e.g.,* the southern portion is frontage, the provision might read as follows:

No partial reconveyance shall be given of any portion of the southerly 150 feet measured at right angles to the southerly boundary until all of the remainder of the property has been partially reconveyed to buyer.

Particular attention should be given to other limitations that may be needed. For instance, releases might need to be made in parcels of at least a certain size, or land not reconveyed and still subject to the seller's lien might have a specified type of access to a dedicated street or highway. Also, care should be taken that access to utilities is preserved. Each parcel has its own unique demands, and the release clause must be shaped to take them into account.

The release provision above conditions the trustor's right to obtain reconveyance on meeting the requirements of the Subdivision Map Act (Govt C §§66410-66499.37). In general, this will require the recordation of a parcel or final map. See §9.103. Because government requirements or the topography may entail irregular lot or parcel boundaries, this form permits the trustor to obtain the release of any legal lot or parcel on payment of the release price for the larger permissible release parcel within which the lot or parcel to be released is situated.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.107 5. Form: Partial Release (Lots Not Determined); Adjustment of Release Price

§9.107 5. Form: Partial Release (Lots Not Determined); Adjustment of Release Price

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§9.105-9.110.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

9.107-1 Partial release (lots not determined); adjustment of release price

[*If appropriate, add to section 3.6 of the purchase and sale agreement (form 4.171-6)*]

Before the close of escrow, Buyer may, at Buyer's option, submit to Seller, for Seller's approval, a proposed division of the property into _ _[*specify number, give maximum or minimum if desired*]**_ _ parcels, to be released from the lien of the Deed of Trust. Buyer's proposed division shall include (a) certification of the total number of gross acres, to the nearest 1/1000th of an acre, within each of the proposed release parcels, addressed to seller and executed by a licensed civil engineer or land surveyor; (b) a legal description of each such parcel; (c) the order of release of such parcels; and (d) a proposed release price for each such parcel. Seller agrees to approve the division proposed by Buyer, as long as the ratio that the fair market value of the land remaining subject to the Deed of Trust after each release bears to the maximum unpaid principal balance of the promissory note is equal to or greater than _ _**[*state a fraction, or specify, e.g., the ratio of the total purchase price to the principal balance of Seller's purchase money note*]**_ _.**

If Seller disapproves of Buyer's proposed division, Seller shall give written notice of disapproval to Buyer within _ _[*number*]**_ _ days after receipt of the proposed division. Seller's notice shall include a proposed new schedule of release prices for each of Buyer's proposed release parcels, which in Seller's opinion result in a ratio that the fair market value of the land to be subject to the Deed of Trust after each such release bears to the maximum unpaid principal balance of the promissory note equal to _ _**[*specify ratio of value of land remaining to balance on note*]**_ _. Seller's failure to give written notice of disapproval to Buyer within _ _**[*number*]**_ _ days shall constitute Seller's approval of Buyer's proposed division of the property and proposed schedule of release prices. If Buyer believes that any of the release prices proposed by Seller are greater than necessary to cause the ratio to be equal to or greater than _ _**[*number*]**_ _, Buyer shall notify Seller of the disagreement, and, if Buyer and Seller cannot resolve their disagreement within _ _**[*number*]**_ _ days after receipt of Buyer's notice, the matter shall be conclusively determined by submitting the dispute to _ _**[*arbitration/appraisal*]**_ _ as follows:**

[*Insert provisions for arbitration or appraisal*]

Fair market value for purposes of this paragraph shall be determined as of _ _[*specify, e.g., the date of this agreement*]**_ _.**

The release parcels and release prices determined under this paragraph shall be inserted into the schedule of release parcels and release prices in the following provision for partial releases, which shall be set forth in the Deed of Trust:

[*Insert last paragraph from form 9.105-1; if appropriate, add paragraph (e) from form 9.106-1 as additional condition to partial releases*]

Comment: In the absence of unfairness, the parties to a contract may agree that the consideration will be determined by disinterested third parties. CC §1610. An option to purchase at a price to be agreed on by the parties was held sufficiently certain to give rise to an enforceable contract in *Bewick v Mecham* (1945) 26 C2d 92, 156 P2d 757, when the agreement also provided that, if the parties could not agree on the purchase price, the price would be fixed by three arbitrators, one to be appointed by each party and the third by the two previously appointed arbitrators. An agreement to surrender shares of stock in a settlement agreement in exchange for payment of an amount equal to the "fair evaluation as agreed by the attorneys" for the parties was held sufficiently certain for specific enforcement in *Forde v Vernbro Corp.* (1963) 218 CA2d 405, 407, 32 CR 577. For a discussion related to the submission of a dispute

to arbitration, see §4.150.

If the buyer and the seller cannot agree on the principal payment required for each partial release and if the seller refuses to permit, or otherwise frustrates, resolution of the dispute by an appraisal or arbitration, the buyer should be able to have the release prices established by the court in an action for specific performance or declaratory relief, particularly if the buyer has changed position in relying on the enforceability of the partial release provision. In *Bewick v Mecham, supra,* the tenant had made building improvements worth $13,500 on leased property in reliance on an option to purchase, and the court determined the purchase price when the defendant-seller refused to appoint an arbitrator. In this situation, if equitable considerations support the position of the party seeking specific performance, the courts tend, as stated in *Bewick,* "to consider these stipulations for a determination of the price by third persons, rather as matters of form than of substance; to construe them in such a manner that they become incidental only to the main object of the agreement. (Pomeroy, Specific Performance of Contracts (3d ed.) §151.)" 26 C2d at 100.

The form provides for the parties to reach an agreement on the release parcels and release prices before the close of escrow. It would also be appropriate to provide that escrow will close despite any dispute over the release prices, or to extend the time to close. The first might be accomplished by including a provision for determination of the release prices by appraisal or arbitration in the deed of trust. The primary disadvantage of this form is the possibility of substantial delay in determining the principal payment required for reconveyance of the release parcels.

Alternative methods of setting the release prices might be used.

EXAMPLE: The release prices might be established by providing that the fair market value of the property to remain subject to the deed of trust must be equal to the maximum unpaid principal balance of the promissory note secured by the deed of trust plus a fixed dollar amount.

Normally, the property should be appraised as of the date the purchase and sale agreement is executed. If, however, subdivision and development will affect the value of different portions of the property, and if the right to obtain releases will be conditioned on subdivision and development, the buyer may want the appraisal to take the different values into account by appraising the property as of a specified later date. In a common interest subdivision, common interest lots will have no independent value; in other subdivisions, property subject to open space restrictions or required to be dedicated for parks or other public purposes may require different treatment.

© The Regents of the University of California

§9.108 6. Form: Unencumbered Conveyance at Close of Escrow

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§9.105-9.110.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

9.108-1 Unencumbered conveyance at close of escrow

[*If appropriate, add to section 3.6 of the purchase and sale agreement (form 4.171-6)*]

At close of escrow and on payment by Buyer to Seller of the sum of _ _[*dollar amount*]**_ _, Seller shall convey free of any lien of Seller that property known as _ _**[*describe land*]**_ _.**

Comment: Often, and particularly when the seller is not subordinating the purchase money deed of trust to liens for construction of other loans (see §§9.66-9.99), the buyer requires the release of some land from the seller's lien. Consideration for acreage released at closing is a matter to be negotiated by the parties. The seller must keep in mind the risk in releasing part of his or her margin of security at this point.

When lots already subdivided are sold, describing the property to be conveyed free of the seller's lien is relatively simple. When undivided acreage is sold, however, describing the property to be released at closing is difficult because the exact acreage of the entire parcel may not be known until a survey is completed (see §§9.106-9.107), and the exact location of those portions the buyer wishes to be conveyed free of any seller's lien cannot be known until preliminary subdivision maps have been prepared. See §9.103. The land to be conveyed free of any seller's lien should be described in language similar to that employed for partial releases after close of escrow (see §§9.105-9.107), and closing should be conditioned on recordation of a parcel or final map that divides the property in such a way that the portion to be conveyed free of the lien of the purchase money deed of trust is a separate lot or parcel.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.109 7. Form: Substituted Security for Releases

§9.109 7. Form: Substituted Security for Releases

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§9.105-9.110.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

9.109-1 Substituted security for releases

[*If appropriate, add to section 3.6 of the purchase and sale agreement (form 4.171-6)*]

The Deed of Trust shall contain the following provision:

After _ _[*insert date of end of seller's tax year of sale*]**_ _, and if no notice of default under this Deed of Trust then appears of record, and after the trustor has paid the maximum payment for the year in which the following arrangement is made, the trustor may obtain partial reconveyances otherwise permissible only in subsequent years by providing security for release payments for the land reconveyed by either (a) delivering to the trustee security for the payment, of a value not less than the security it replaces and of a nature and on terms reasonably approved by the beneficiary; or (b) depositing with the trustee under the Deed of Trust as a pledge and as security for the payment personal property of the following kind of a face value not less than the balance then due the beneficiary, including interest accrued to date of the deposit, plus _ _**[*specify additional amount*]**_ _:**

(1) United States or State of California bonds, legal for use as collateral, as long as they are then currently selling at not less than face value;

(2) Deposit books or time deposits of any _ _[*name*]**_ _ County branch of a bank or savings and loan association whose deposits are insured by an agency of the federal government, as long as the limit of deposit insurance shall not be exceeded for any bank or savings and loan association without Seller's consent, in its sole and absolute discretion;**

(3) Other stocks or bonds that are readily marketable on a national exchange and hold not less than the following credit rating _ _[*specify*]**_ _, as long as Buyer shall at all times maintain a value ratio compared to the dollar amount of the obligation to be replaced of at least the following: _ _**[*number*]**_ _ to 1; or**

(4) Any combination of the above.

The deposit shall be made and held subject to the terms of a pledge agreement executed by the trustor, the trustee, and the beneficiary before recordation of this Deed of Trust. Subject to the lien of the pledge, the trustor shall retain ownership of the pledged property, and any increment of interest on it, and shall not permit or cause the substituted security to be subjected to any impairment, levy, or claim.

Comment: Although the seller may want to limit annual payments in order to spread his or her tax deferral over as long a period as possible (see §9.24), the buyer may require reconveyances sooner than the payment schedule permits, especially when the development is successful. If other security is substituted for the land reconveyed, the buyer's purpose is achieved. If the security is of sufficient value, the seller's right to ultimate payment is not jeopardized. Substitution of a cash equivalent as security under a pledge agreement may reduce the seller's risk that he or she will have received reportable income. In *J. Earl Oden* (1971) 56 TC 569, however, installment reporting was held unavailable when the buyer merely deposited certificates of deposit into escrow at the time of sale and the parties intended that the certificates constitute payment rather than security. See also Rev Rul 77-294, 1977-2 Cum Bull 173, amplified by Rev Rul 79-91, 1979-1 Cum Bull 179. For further discussion of constructive receipt problems with cash equivalents held as substituted security, see Greene & Share, *Starker and Beyond: Including the Uncertain Life of Secured Deferred Exchange*, 58 Taxes 724, 732 (1980).

A title company may act as a pledge holder, as long as it approves the form of the pledge agreement. The terms of the pledge agreement should be agreed on before the purchase agreement is executed, and a copy of the pledge agreement should be attached to the purchase agreement. The pledge agreement should provide that the pledged property is held as security for payment of the unpaid portion of the release price and that the pledgor is personally liable for payment.

In *David Dobrich* (1997) TC Memo 1997-477, sellers were not entitled to use installment reporting of gains recognized from the disposition of real property due to failure to comply with the tax-deferred exchange requirements of IRC §1031.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/9 Seller Financing/§9.110 8. Form: Release on Condemnation Award

§9.110 8. Form: Release on Condemnation Award

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§9.105-9.110.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

9.110-1 Release on condemnation award

[*If appropriate, add to section 3.6 of the purchase and sale agreement (form 4.171-6)*]

The Deed of Trust shall contain the following provision:

If any award of damages is made for condemnation affecting any part of the property subject to this Deed of Trust and if at the time of the award the trustor has the right to demand reconveyance on payment of a specific sum, the trustor shall pay that sum to the beneficiary and shall then be entitled to receive the award. If any damages award is made for any other portion of the property subject to this Deed of Trust, the beneficiary shall receive the proportion of the award that the balance then due the beneficiary bears to the market value of the entire parcel subject to the Deed of Trust at the date of the award. If the market value of the entire parcel cannot be agreed on by the trustor and the beneficiary, it shall be determined by appraisal as provided in paragraph _ _ _.

Comment: Complications may arise if the property is condemned after close of escrow when the seller's rights in the property are those of an encumbrancer. The agreement and the security instrument should provide for these rights.

If the entire parcel is condemned, there is usually no problem, because the lienholder receives the amount due on the lien from the award, which is generally sufficient for this purpose. See Condemnation Practice in California §10.16 (3d ed Cal CEB 2005). The problem is also minimized if a partial taking affects a portion of the property that may itself be reconveyed under other provisions of the instrument (a specific lot, *e.g.,* under provisions as in §9.105). In a partial taking under CCP §1265.225, the lienholder shares in the award only to the extent that the security is impaired. See Condemnation Prac §12.23. However, the taking under condemnation may include property not yet subject to release because other property must first be released (see Comment in §9.106), or the taking may impair the value of the remaining land because of severance damages, the irregularity of the taking, or other factors. Most standard deed of trust forms permit the beneficiary to receive all proceeds of any award, although such a provision might be held to be subject to an implied covenant of good faith on the part of the beneficiary. See *Milstein v Security Pac. Nat'l Bank* (1972) 27 CA3d 482, 103 CR 16. The form divides the award in proportion to the parties' financial interests. As between buyer and seller, such a provision is subject to variations in allocation to suit the particular situation.

© The Regents of the University of California

10

Deeds

Scott A. Sommer

I. REQUISITES OF DEEDS
- A. Legal Definitions §10.1
- B. Types of Deeds
  - 1. Grant Deed
    - a. Features and Incidentals of the Grant §10.2
    - b. Form: Statutory Grant Deed Form (CC §1092) §10.3
  - 2. Quitclaim Deed §10.4
  - 3. Warranty Deed §10.5
- C. Necessary Elements of Deeds §10.6

II. COMPONENTS ANALYZED
- A. Form: Grant Deed §10.7
- B. Recording Information
  - 1. "Recording Requested By" §10.8
  - 2. Return Name and Address §10.9
  - 3. Tax Statements §10.10
  - 4. Documentary Transfer Tax
    - a. Statutory Requirements §10.11
    - b. Form: Separate Statement of Documentary Transfer Tax §10.12
- C. Body of Deed
  - 1. Consideration §10.13
  - 2. Grantor Recitals §10.14
    - a. Form: Grantor's Name Different From Record Owner's Name §10.15
    - b. Form: Unincorporated Association §10.16
    - c. Form: Partnership §10.17
    - d. Form: Limited Partnership §10.18
    - e. Form: Trustee §10.19
    - f. Form: Corporation §10.20
    - g. Form: Joint Venture §10.21
    - h. Other Grantor Clauses §10.22
  - 3. Words of Conveyance §10.23
  - 4. Grantee
    - a. Requirement of Capacity §10.24
    - b. Requirement of Certainty §10.25
    - c. Status of Grantee §10.26
    - d. Other Required Elements §10.27
      - (1) Nature of Estate §10.28
      - (2) Nature of Ownership §10.29
      - (3) Proportion of Interest §10.30
    - e. Grantee Recitals
      - (1) Form: Joint Tenancy §10.31
      - (2) Form: Tenancy in Common §10.32
      - (3) Form: Community Property §10.33
      - (4) Form: Changing Title From Joint Tenancy to Community Property §10.34
  - 5. Description §10.35
  - 6. Exhibits and Riders §10.36
  - 7. "Subject to" Clauses §10.37
  - 8. Special Recitals §10.38
    - a. Form: Spouse-to-Spouse Recital of Separate Property §10.39
    - b. Form: Consent to Joint Tenancy Between One Spouse and Another Person §10.40
    - c. Form: Deed in Lieu of Foreclosure §10.41
    - d. Correcting, Removing, and Releasing Recitals
      - (1) Form: Correcting or Clarifying Description of Property §10.42

(2) Form: Removing Cloud on Title §10.43
(3) Form: Release of Exception or Reservation §10.44
e. Compliance With Obligation Recitals
(1) Form: Conveyance in Performance of Sales Agreement §10.45
(2) Form: Conveyance on Exercise of Option §10.46
(3) Form: Conveyance on Distribution of Trust §10.47
f. Termination Recitals
(1) Form: Termination of Recorded Lease §10.48
(2) Form: Elimination of Covenants, Conditions, and Restrictions §10.49
(3) Form: Removal of Power of Termination §10.50
g. Reservation Recitals
(1) Form: Mineral Rights §10.51
(2) Form: Life Estate §10.52
D. Execution
1. Date of Execution §10.53
2. Definition §10.54
3. Requirements
a. Who Signs §10.55
b. Spouse's Signature §10.56
c. Homestead Declaration §10.57
d. Termination of Joint Tenancy §10.58
4. Particular Executions
a. Form: Mark of Executing Party §10.59
b. Form: Signature of Attorney-in-Fact §10.60
c. Form: Signature of Trustee §10.61
d. Form: Signature of Guardian or Conservator §10.62
e. Form: Signature of Executor or Administrator §10.63
f. Form: Signature of Partner §10.64
g. Form: Signature of Corporate Officer §10.65
h. Form: Signature of Joint Venturer §10.66
E. Acknowledgment
1. Legal Requirements §10.67
2. Documents That Need Not Be Acknowledged §10.68
3. Effect of Acknowledgment §10.69
4. Proof of Unacknowledged Documents §10.70
F. Delivery §10.71
1. Unconditional Delivery Is Required §10.72
2. Rebuttable Presumptions on Delivery §10.73
3. Constructive Delivery §10.74
G. Acceptance §10.75

III. VALIDITY OF DEEDS
A. Void Deeds §10.76
B. Voidable Deeds §10.77

© The Regents of the University of California

I. REQUISITES OF DEEDS

§10.1 A. Legal Definitions

An estate in real property, other than an estate at will or for a term not exceeding 1 year, can be transferred only by operation of law, or by an instrument in writing, signed by the party disposing of the property or that party's agent duly authorized by writing. CC §1091. Leases for longer than 1 year must also be in writing under the Statute of Frauds. CC §1624(a)(3).

A transfer in writing of an estate in real property is called a grant or a conveyance. CC §§1039, 1053. The grant takes effect between the parties when delivered. CC §1054. A grant that has been duly executed is presumed delivered at its date of execution. CC §1055. See also §10.53. Delivery of the deed is absolute, except that delivery can be on performance of a condition, in which event it is termed an escrow. CC §1057. A mere possibility, not coupled with an interest, cannot be transferred. CC §1045. The term "conveyance" includes every instrument in writing by which any estate or interest in real property is created, alienated, mortgaged, encumbered, or affected, except wills. CC §1215.

A conveyance, when duly acknowledged and recorded, imparts constructive notice under the Recording Act. CC §1213. Unrecorded instruments are valid only between the parties to the instrument and those who have notice of it. CC §1217.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/ B. Types of Deeds/ 1. Grant Deed/§10.2 a. Features and Incidentals of the Grant

B. Types of Deeds

1. Grant Deed

§10.2 a. Features and Incidentals of the Grant

A grant deed is characterized by use of the word "grant" as the operative word of conveyance. CC §1092. The word "grant" in the deed implies covenants that (CC §1113)

- the grantor has not conveyed the same estate to anyone other than the grantee; and
- the property is free of encumbrances placed on the property or suffered by the grantor (see §§12.5-12.7).

If the grantor acquires title to the property after executing a grant deed conveying the property to another, such after-acquired title passes to the grantee by operation of law (CC §1106) and inures to the benefit of a mortgagee (CC §2930).

NOTE: Transfers of one to four dwelling units or residential condominiums require disclosures under CC §§1102-1102.17, 1103-1103.4, 1134. See §§5.7, 5.24.

With deeds, as in any contract, the primary object of interpretation is to ascertain and carry out the intention of the parties. *City of Manhattan Beach v Superior Court* (1996) 13 C4th 232, 238, 52 CR2d 82. The deed may be construed in light of extrinsic evidence that may prove a meaning to which the language of the instrument is reasonably susceptible. 13 C4th at 238; *City & County of San Francisco v Union Pac. R.R. Co.* (1996) 50 CA4th 987, 994, 58 CR2d 1.

References to land in a deed, particularly those containing precise technical descriptions, are generally interpreted as an intent to transfer the entire estate. *City of Manhattan Beach,* 13 C4th at 244; *Severns v Union Pac. R.R. Co.* (2002) 101 CA4th 1209, 1215, 125 CR2d 100. It will be presumed that a grant was intended to pass a fee simple title unless it appears from the grant that a lesser estate was intended. *Union Pac. R.R. Co.,* 50 CA4th at 995. A quitclaim deed transfers whatever present right or interest the grantor has in the property. *City of Manhattan Beach v Superior Court, supra*.

A transfer of real property passes all easements attached to it, even if not expressly included in the grant, and creates an easement to use other real property of the transferor to the same extent as such other property was obviously and permanently used at the time of the transfer. CC §1104; *Kytasty v Godwin* (1980) 102 CA3d 762, 771, 162 CR 556. An implied easement must be reasonably necessary to the use and benefit of the quasi-dominant tenement and will not be found absent clear evidence that it was intended by the parties. *Tusher v Gabrielsen* (1998) 68 CA4th 131, 80 CR2d 126. A deed conveying a parcel by reference to a recorded parcel map is deemed to incorporate any prior properly recorded amendment to the map not expressly recited. *Christian v Flora* (2008) 164 CA4th 539, 554, 78 CR3d 892. Water rights are considered appurtenant and are presumed transferred with the land absent express reservation. *Nicoll v Rudnick* (2008) 160 CA4th 550, 558, 72 CR3d 879. On easements generally and those relating to water rights, see California Easements and Boundaries: Law and Litigation (Cal CEB 2008).

When property is acquired by a public entity through private dedication, the deed is strictly construed and a public trust—distinct from the public trust applicable to tidelands—is applicable to enjoin use of the property contrary to the dedicated purpose set forth in the grant. *County of Solano v Handlery* (2007) 155 CA4th 566, 576, 66 CR3d 201. On public trust tideland issues, see Easements, chap 3; California Land Use Practice, chap 14 (Cal CEB 2006).

As noted above, fee simple title is presumed to pass by a grant unless it appears from the grant that a lesser estate was intended. CC §1105. The description in a deed as to the form of title is presumed to reflect the actual ownership interest in the property, which may be rebutted only by clear and convincing proof. *Marriage of Brooks & Robinson* (2008) 169 CA4th 176, 184, 86 CR3d 624; Evid C §662. The grant is conclusive on the grantor and against everyone subsequently claiming under the grantors except a purchaser or mortgagee in good faith and for a valuable consideration who acquires a title or lien by a conveyance that is first duly recorded. CC §1214. *Triple A Mgmt. Co. v*

Frisone (1999) 69 CA4th 520, 81 CR2d 669; *First Fid. Thrift & Loan Ass'n v Alliance Bank* (1998) 60 CA4th 1433, 71 CR2d 295. A good faith purchaser and encumbrancer must act without knowledge or notice of facts sufficient to raise a duty of inquiry by a reasonable and prudent person. *Triple A Mgmt. Co.,* 69 CA4th at 530.

A grant by the owner of a life estate or term of years in excess of the estate that he or she could lawfully transfer does not work a forfeiture, but passes all the estate he or she could lawfully transfer. CC §1108.

A grant made on a condition subsequent is defeated by nonperformance of the condition, and the person entitled to hold under the grant must reconvey the property to the grantor or his or her successors. CC §1109. If the grant is made to take effect on performance of a condition precedent, it passes the estate on performance of the condition (CC §1110; but note effect of recording statute, CC §§1213-1220).

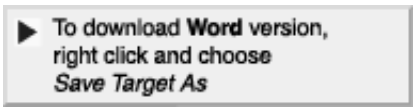
Note that a conveyance subject to restrictions on use imposed as part of a common interest subdivision is presumed reasonable under CC §1354(a). *Nahrstedt v Lakeside Village Condominium Ass'n* (1994) 8 C4th 361, 372, 33 CR2d 63, 87. *Harvey v The Landing Homeowners Ass'n* (2008) 162 CA4th 809, 817, 76 CR3d 41; *Fourth La Costa Condominium Owners Ass'n v Seith* (2008) 159 CA4th 563, 576, 71 CR3d 299. The person attacking the restriction bears the burden of proving that it is unreasonable. *Colony Hill v Ghamaty* (2006) 143 CA4th 1156, 1165, 50 CR3d 247.

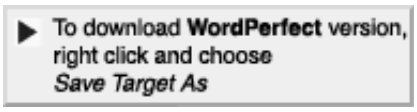
For a form grant deed, see App G.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.3 b. Form: Statutory Grant Deed Form (CC §1092)

§10.3 b. Form: Statutory Grant Deed Form (CC §1092)





10.3-1 Statutory grant deed form

I, *A B*, grant to *C D* all that real property situated in _ _[*name*]_ _ County, State of California, bounded (or described) as follows: _ _[*describe*]_ _.

Witness my hand this _ _[*insert day*]_ _ day of _ _[*insert month*]_ _, _ _[*year*]_ _.

A B

Comment: This grant deed form is prescribed by CC §1092. This statutory form need not be used; even a badly worded instrument can operate to convey property if the intention to make a present transfer of real property is evident from it. See *Olson v Cornwell* (1933) 134 CA 419, 25 P2d 879. However, for the writing to be given effect as a deed, it must satisfy the requisites listed in §10.6.

© The Regents of the University of California

§10.4 2. Quitclaim Deed

A quitclaim deed, commonly used in California, is derived from the common law release and is characterized by the operative words "remise, release, and quitclaim" or merely "quitclaim." It transfers only whatever interest, legal or equitable, the grantor has at the time of its execution, without any implied covenants concerning title or encumbrances. *Marriage of Goia* (2004) 119 CA4th 272, 280, 14 CR3d 362; *Klamath Land & Cattle Co. v Roemer* (1970) 12 CA3d 613, 91 CR 112.

A quitclaim deed, unlike a grant deed conveying the fee interest, does not pass after-acquired title to the grantee by operation of law. See *Johnson v E-Z Ins. Brokerage, Inc.* (2009) 175 CA4th 86, 94, 95 CR3d 782; *Klamath Land & Cattle Co. v Roemer, supra; Taylor v Coachella Valley County Water Dist*. (1952) 108 CA2d 743, 239 P2d 454. The grantee of a quitclaim deed can be a bona fide purchaser and is protected from unrecorded instruments affecting title, including grant deeds. *Beach v Faust* (1935) 2 C2d 290, 40 P2d 822.

© The Regents of the University of California

§10.5 3. Warranty Deed

Warranty deeds contain express covenants, such as covenants against encumbrances and of quiet enjoyment. They are rarely used in California because a grant deed, combined with a title insurance policy, is generally considered sufficient protection for buyers. See 3 Miller & Starr, California Real Estate §8:11 (3d ed 2000). For a form of warranty deed covenants, see §12.12.

© The Regents of the University of California

§10.6 C. Necessary Elements of Deeds

To be valid, a deed of any type must contain each of the following requisites:

- A sufficient writing (CC §§1053, 1091) bearing the names of the grantor and grantee (see §§10.14-10.22, 10.24-10.34), operative words of conveyance (see §10.23), and a sufficient description of the property (see §10.35);
- Competent parties (see §§10.14, 10.24);
- Property interests that may be legally transferred (see §10.1);
- Proper execution (see §§10.59-10.66); and
- Delivery and acceptance (see §§10.71-10.75).

Generally, consideration is not essential to the validity of a deed (see §10.13). Recording is not essential to a deed's validity as between grantor and grantee and against those with notice of its existence. CC §1217; *Chaffee v Sorensen* (1951) 107 CA2d 284, 236 P2d 851. Acknowledgment is necessary if the deed is to be recorded, but it is not essential to the deed's validity except in the case of a conveyance of a married person's homestead. Instruments defectively acknowledged or executed but nonetheless recorded impart constructive notice 1 year after recordation. CC §1207. See §§10.67-10.70 for discussion of acknowledgments.

© The Regents of the University of California

II. COMPONENTS ANALYZED

§10.7 A. Form: Grant Deed

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.7-1 Grant deed

RECORDING REQUESTED BY)
[*see §10.8*] **)**
WHEN RECORDED MAIL TO)
[*see §10.9*] **)**
MAIL TAX STATEMENTS TO)
[*see §10.10*] **)**
_____)

GRANT DEED

The undersigned grantor(s) declare(s) [*see §§10.11-10.12*]**:**

Documentary transfer tax is _ _[*dollar amount*]**_ _.**

[ ] **Computed on full value of property conveyed, or**

[ ] **Computed on full value less value of liens and encumbrances remaining at time of sale.**

[ ] **Unincorporated area:** [ ] **City of _ _**[*name*]**_ _, and**

FOR A VALUABLE CONSIDERATION, receipt of which is hereby acknowledged [*see §10.13*]**, _ _**[*names of grantors; see §§10.14-10.22*]**_ _ hereby GRANT(S)** [*see §10.23*] **to _ _**[*names of grantees; see §§10.24-10.34*]**_ _ the following described real property in the _ _**[*City of _ _*[*name*]*_ _,/City and*]**_ _ County of _ _**[*name*]**_ _, California:**

[*Insert property description; see §10.35. On "subject to" clauses, see §10.37; on special recitals, see §§10.38-10.52*]

Date: _ _[*see §10.53*]**_ _** **__**[*Execution; see §§10.54-10.66*]**__**

[*Acknowledgment; see §§10.67-10.70*]

[*Seal*]

MAIL TAX STATEMENTS AS DIRECTED ABOVE [*see §10.10*]

Comment: This form is an example of available form deeds. Grant deed forms are available from title companies and stationery stores. The various components of deeds are discussed in the sections that follow, as cross-referenced in the body of the deed.

The form clauses in §§10.15-10.52 are set out and discussed to assist the drafter in meeting specific problems. They may be included either in a separately drafted deed or by amending a form deed if space permits.

For another form grant deed, see App G.

© The Regents of the University of California

B. Recording Information

§10.8 1. "Recording Requested By"

Under Govt C §27320, the name of the person at whose request the document is recorded must be noted. "Grantee," "beneficiary," and "vendee," in place of the name of a person, are not sufficient. "Recording requested by" or its equivalent, and the name of the requesting person, must appear on the face of the document. The space in the upper left-hand corner of the document, measuring at least 2½ inches vertically by 3½ inches horizontally, must be reserved to show the name of the person requesting recordation and the return name and address discussed in §10.9. Govt C §27361.6.

© The Regents of the University of California

§10.9 2. Return Name and Address

The recorder must mail (or deliver if specified) the instrument to the person named in the instrument for return mail and, if no one is named, to the person leaving it for recording. Govt C §27321. To enable the recorder to comply, a return name and address should appear on each instrument to be recorded. On the location of this information, see §10.8.

If the instrument effects a change of ownership, a change of ownership statement (Rev & T C §480) should accompany the recorded document. Govt C §27321.

NOTE: The return name and address is used for notices in nonjudicial foreclosure proceedings (CC §2924b(c)(1)), judicial foreclosure proceedings (CCP §726(c)), and enforcement of judgments (CCP §701.540(h)).

© The Regents of the University of California

§10.10 3. Tax Statements

Before it will be accepted for recording, every deed or instrument executed to convey fee title to real property must have written across the bottom of the first page the name and address to which future tax statements may be mailed. Govt C §27321.5.

There are four acceptable ways to comply with §27321.5:

(1) The bottom of the first page may be worded as follows:

Mail tax statements to _ _[*name*]_ _, _ _[*address*]_ _.

(2) The tax name and address may be located below the recording address, with the wording across the bottom of the first page as follows:

Mail tax statements as directed above.

(3) When the return name and address (see §10.9) are the same as that to which future tax statements are to be mailed, the following wording may be used across the bottom of the first page:

Mail tax statements to the return address above.

(4) If the deed does not convey fee title to real property, tax information is not required. Govt C §27321.5. In this event, "does not convey fee title" must appear in either the heading or the body of the deed.

If a life estate, an estate for years, or an estate at will is conveyed, the deed must recite "does not convey fee title," because these are not estates of inheritance (CC §761) and thus are not fee estates under CC §762.

© The Regents of the University of California

4. Documentary Transfer Tax

§10.11 a. Statutory Requirements

Under the Documentary Transfer Tax Act (Rev & T C §§11901-11934), cities and counties may by ordinance impose a tax on each deed or other instrument transferring real property. Subject to certain exemptions (Rev & T C §§11921-11930), the tax is imposed on deeds when the purchase price or the value of the interest or property conveyed, less the value of any liens or encumbrances remaining on it at the time of sale, exceeds $100. Rev & T C §11911(b). Although the statutory language is not entirely clear, this provision is generally construed to impose the tax on the amount of the transferee's equity in the real property, *i.e.,* the cash consideration. The maximum allowable tax rate is $.55 per $500 of the property's value, less the value of any remaining liens and encumbrances. If the land is within a city that has enacted a tax, one-half of that amount goes to the city and the remainder goes to the county, if it has imposed a tax. Rev & T C §11911. Charter cities can charge an additional transfer tax over and above the tax charged by the county. *Cohn v City of Oakland* (1990) 223 CA3d 261, 272, 272 CR 714. The tax is collected by the county recorder; the county auditor allocates it between the county and the city. Rev & T C §11931. The tax must be paid before the instrument will be recorded, although constructive notice is not affected if, in fact, collection of the tax fails. Rev & T C §11933. The face of a deed submitted for recordation must show the amount of the tax due and the location of the real property, except that the party submitting the document may provide that information on a separate document to be attached to the deed after recording and before return to the party. Rev & T C §11932. See §10.12 for a form for a separate document providing the documentary transfer tax information.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.12 b. Form: Separate Statement of Documentary Transfer Tax

§10.12 b. Form: Separate Statement of Documentary Transfer Tax

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.12-1 Separate statement of documentary transfer tax

_ _[*Name*]_ _**, County Recorder**
_ _[*Name of county*]_ _
_ _[*Address*]_ _

Dear _ _[*name*]_ _**:**

In accordance with Revenue and Taxation Code §11932, it is requested that this statement of documentary transfer tax due not be recorded with the attached deed but be affixed to the deed after recordation and before return as directed on the deed.

The deed names _ _[*name*]_ _ **as grantor and** _ _[*name*]_ _ **as grantee. The property being transferred is located in** _ _[*name of city; specify if in unincorporated area of county*]_ _**.**

The amount of documentary transfer tax due on the attached deed is _ _[*dollar amount*]_ _**, computed on the full value of the property** _ _[*less any encumbrances remaining on the property*]_ _**.**

Comment: Because the documentary transfer tax varies with the value of the property, its disclosure on the deed enables third parties to calculate the amount paid for the property. If the buyer wishes to avoid disclosing the price paid, this procedure may be followed. When this form is used, the deed should contain a statement that the amount of tax due is shown on a separate writing and is not for public record.

© The Regents of the University of California

C. Body of Deed

§10.13 1. Consideration

Consideration is not necessary for a voluntary transfer. CC §1040. A written instrument is presumptive evidence of consideration. CC §1614. "For a valuable consideration" is superfluous language. *Goad v Moulton* (1885) 67 C 536, 8 P 63. In deeds made by administrators, executors, guardians, trustees, and receivers who are conveying property under court order, title insurers sometimes require that the deeds recite the exact amount of consideration received. Some title insurers require consideration to be recited in deeds made by trustees not acting under court order, attorneys-in-fact, municipal corporations, or other public agencies.

Whether there was consideration for a conveyance may, however, have important consequences for the parties:

- Primarily, valuable consideration is necessary to give a recorded deed priority over an earlier unrecorded deed. CC §1214.
- A conveyance without a fair consideration that is made at a time when the grantor is insolvent, or that leaves the grantor insolvent, may be fraudulent toward creditors. If there is no purchaser, encumbrancer, or successor in interest for a fair consideration and without knowledge of the fraud, the creditors can have the deed set aside. See *Kirkland v Risso* (1979) 98 CA3d 971, 159 CR 798; *Stearns v Los Angeles Sch. Dist.* (1966) 244 CA2d 696, 53 CR 482. California has adopted the Uniform Fraudulent Transfer Act (UFTA) (CC §§3439-3449), effective January 1, 1987, for transfers made or obligations incurred on or after that date only, and repealed the former Uniform Fraudulent Conveyance Act. However, the former Act (former CC §§3439-3439.12) still applies to transfers made or obligations incurred during the former Act's existence. In addition to the UFTA, fraudulent conveyances and transfers may also be challenged on common law grounds. See *Macedo v Bosio* (2001) 86 CA4th 1044, 104 CR2d 1. The UFTA applies to property transfers between spouses pursuant to dissolution judgments or marital settlement agreements. *Mejia v Reed* (2003) 31 C4th 657, 669, 3 CR3d 390.
- A deed without consideration may be considered a gift deed and may be subject to federal gift taxes (IRC §2512(b)) or federal estate taxes (IRC §2035).
- The law will not imply a covenant against encumbrances from a gift deed. *Estate of Porter* (1903) 138 C 618, 72 P 173.
- Both valuable consideration and lack of notice are necessary for a purchaser to take good title free of any claim that an earlier transaction, although absolute on its face, was a mortgage. CC §2925.
- A nominal amount of consideration may be extrinsic evidence affecting interpretation of the grant. See *Warren v Atchison, T. & S.F. Ry*. (1971) 19 CA3d 24, 35, 96 CR 317 (easement instead of a fee); *Munger v Moore* (1970) 11 CA3d 1, 89 CR 323 (deed absolute interpreted as a mortgage); *Rickless v Temple* (1970) 4 CA3d 869, 84 CR 828 (deed absolute interpreted as a mortgage).
- Lack of consideration may result in a trust in favor of the grantor. *Lehmann v Kamp* (1969) 273 CA2d 701, 77 CR 910.
- A paper transfer without consideration is one indicator of ownership to be considered when a local government wishes to merge contiguous substandard parcels pursuant to Govt C §66451.11. *Kalway v City of Berkeley* (2007) 151 CA4th 827, 60 CR3d 477 ("paper transfer" was not authorized by Subdivision Map Act, but Act does not authorize setting aside deed; nevertheless, grantee has no right to further transfer deed).

© The Regents of the University of California

§10.14 2. Grantor Recitals

The body of the deed must contain the grantor's name or such other description to sufficiently identify the grantor. "I, the undersigned," is permissible; the style in the 19th and early 20th century was to establish the grantor as the "party of the first part." See *Childs v Newfield* (1934) 136 CA 217, 28 P2d 924.

See §§4.14-4.18 on the capacity of grantors. For discussion of discrepancy between the grantor name in the body of the deed and the execution name, see §§10.15, 10.55-10.56.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.15 a. Form: Grantor's Name Different From Record Owner's Name

§10.15 a. Form: Grantor's Name Different From Record Owner's Name

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.15-10.21.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.15-1 Grantor's name different from record owner's name

[*Add one of the following alternatives*]

[*Alternative 1: Grantor's name different from record owner's name*]

_ _[*Name(s) of grantor(s)*]_ _**, also known as** _ _[*name under which title held*]_ _**,**

[*Alternative 2: Grantor's name different from record owner's name (same person who acquired title)*]

_ _[*Name of grantor*]_ _**, being the same person who acquired title as** _ _[*name under which title held*]_ _**,**

[*Alternative 3: Grantor's name different from record owner's name (title acquired under former name)*]

_ _[*Name of grantor*]_ _**, who acquired title to the property described below under** _ _[*his/her*]_ _ **former name of** _ _[*name under which title held*]_ _**,**

[*Continue*]

Comment: If a person has record title to real property in one name and later changes his or her name, whether by court action (CCP §§1275-1279.6) or otherwise, the name in which he or she derived title to the property must be stated. If this is not done, the conveyance, though recorded, does not impart constructive notice under CC §1096; it is valid, however, between the parties. See CC §§1096, 1217. Unless the name of the grantor in the deed is substantially identical to the name of the record owner (creating presumption of identity of person), the title is not marketable. *Benson v Shotwell* (1890) 87 C 49, 25 P 249.

A longer statement is sometimes used:

EXAMPLE: "*AB*, being the person formerly known as *CD*, her name having been changed by a final judgment of the Superior Court of the State of California, County of Los Angeles, in Case No. 00000…."

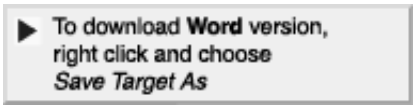
This version is preferable in that it aids third parties and title insurers in establishing a valid chain of title. Care should be taken to verify that the case name and number are stated correctly; if they are not, a certified copy of the decree could be recorded concurrently with the deed.

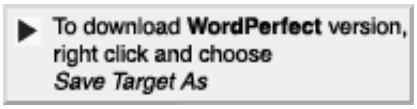
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.16 b. Form: Unincorporated Association

§10.16 b. Form: Unincorporated Association

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.15-10.21.





10.16-1 Unincorporated association

_ _[*Name of organization*]_ _**,** _ _[*e.g., a lodge/a branch*]_ _ **of** _ _[*name*]_ _**, an unincorporated** _ _[*e.g., society, association, labor organization*]_ _**,**

Comment: Traditionally, in California, the property of an unincorporated association belonged to its members. CC §1362; *Grand Grove of United Ancient Order of Druids v Garibaldi Grove No. 71* (1900) 130 C 116, 62 P 486; *County of Trinity v Rourke* (1969) 275 CA2d 628, 79 CR 902. Because the property of an unincorporated association was considered to belong to its members, the association itself could not hold title to or convey real property. This rule has been ameliorated by statutes that now provide that an unincorporated society, association, or labor organization (Corp C §18105), and certain medical associations (Corp C §21200), may acquire title to real property. A conveyance of real property by an unincorporated benevolent or fraternal association or labor organization must be executed by its presiding officer and recording secretary under its seal after a resolution has been duly adopted by the association authorizing the conveyance. Corp C §18120. In the case of other unincorporated associations, the conveyance must be executed by its president and secretary, by other comparable officers, or by other officers specifically designated by a duly adopted resolution.

If an unincorporated association does not fall within the purview of Corp C §§18105 and 18120, its trustees can convey title for it if title is recorded in their names. See §10.20. Otherwise, the individual members should be named as grantors. Therefore, reference in the deed to the association is unnecessary and is useful only for identification.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.17 c. Form: Partnership

§10.17 c. Form: Partnership

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.15-10.21.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.17-1 General partnership

_ _[*Name of partnership*]_ _**, a partnership,**

Comment: In September 1996, California enacted the Uniform Partnership Act of 1994 (UPA), which governs all general partnerships as of January 1, 1999. UPA is located in Corp C §§16100-16962.

An estate in real property, acquired in the partnership name, can be conveyed only in the partnership name. Corp C §§16203-16204, 16501. Title companies usually require recordation under Corp C §16303 of a statement of a general partnership authority. Conveyance of an estate of real property owned by a partnership but held in the names of the partners is governed by Corp C §§16301-16302.

A grant of authority to transfer real property held in the name of a partnership contained in a certified copy of a filed statement of partnership authority recorded in the office for recording transfers of that real property is conclusive in favor of a person who gives value without knowledge to the contrary, as long as a certified copy of a filed statement containing a limitation on that authority is not then of record. Corp C §§16105, 16303(d)(2). See *Federal Deposit Ins. Corp. v Superior Court* (1997) 54 CA4th 337, 62 CR2d 713.

© The Regents of the University of California

§10.18 d. Form: Limited Partnership

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.15-10.21.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.18-1 Limited partnership

_ _[*Name of limited partnership*]_ _**, a limited partnership**

Comment: Limited partnerships formed on or after July 1, 1984, are governed by the California Revised Limited Partnership Act (Revised Act) (Corp C §§15611-15724) (repealed operative 1/1/10). Limited partnerships formed before that date are governed by the California Uniform Limited Partnership Act (ULPA) (Corp C §§15501-15533) unless the partnership elects to be governed by the Revised Act. Corp C §15712(b)(1). Limited partnerships formed after January 1, 2008, are governed by the Uniform Limited Partnership Act of 2008 (ULPA) (Corp C §§15900-15912.07); limited partnerships in existence before that date may elect to be governed by its provisions as of January 1, 2007. Corp C §15912.06(a)(2). Note that the "old" ULPA will no longer govern pre-1984 limited partnerships after December 31, 2009; as of January 1, 2010, *all* California limited partnerships will be subject to the 2008 ULPA regardless of formation date. See §4.25; Advising California Partnerships §§5.7-5.8 (3d ed Cal CEB 1999).

Title companies usually require that a certificate of limited partnership (Corp C §§15621 (Corp C §15902.01, operative Jan. 1, 2008, for new or electing limited partnerships)) be recorded before the title company will insure title of a limited partnership.

On limited partnerships and limited liability partnerships taking title, see §§4.25-4.26.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.19 e. Form: Trustee

§10.19 e. Form: Trustee

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.15-10.21.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.19-1 Trustee

_ _[*Name(s) of trustee(s)*]_ _**, as trustee(s)** _ _[*for* _ _[*name*]_ _*, under the will of* _ _[*name*]_ _*, deceased/under the trust agreement dated* _ _[*date*]_ _**,** *between* _ _[*name*]_ _ *and* _ _[*name*]_ _]_ _**,**

Comment: This form is suitable for naming a trustee, under a will or by inter vivos trust, as grantor.

To the extent an estate fiduciary uses the court-supervised confirmation of sale procedures to sell real property, Prob C §7263 provides that a certified copy of the order confirming the sale be recorded in the office of the county recorder of each county in which the land, or any part of it, lies.

Signatures of trustees who signed only as *individuals*—and not as trustees—are not sufficient to convey good title from a revocable inter vivos trust when all the trustees signed the deed and the trustees were also the beneficiaries with the power to direct the sale of the property. *Galdjie v Darwish* (2003) 113 CA4th 1331, 7 CR3d 178.

PRACTICE TIP: The recital of the date of the trust agreement and of the names of the trustors of an inter vivos trust is unnecessary if the transfer to the trustee is of record. It is common practice, however, to make these recitals because trustees feel more comfortable if the source of their authority is stated.

A constructive trust may be imposed notwithstanding the form of a deed if title was obtained by actual fraud, mistake, or constructive fraud through violation of a fiduciary or confidential relationship. *Warren v Merrill* (2006) 143 CA4th 96, 49 CR3d 122.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.20 f. Form: Corporation

§10.20 f. Form: Corporation

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.15-10.21.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.20-1 Corporation

_ _[*Name of corporation*]_ _**, a** _ _[*name of state of incorporation*]_ _ **corporation,**

[*Add if corporation changed name after acquiring title*]

successor by _ _[*manner of succession*]_ _ **to** _ _[*name of predecessor corporation*]_ _**,**

Comment: California corporations have the power to acquire and convey real property (see §4.28). Corp C §207. Foreign corporations can also acquire and convey California real property. Corp C §208. Naming the place of incorporation is customary practice in identifying the grantor corporation, although it is unnecessary if the property is of record in the grantor's name.

If the corporation changed its name after acquiring title to real property, it will be subject to CC §1096 when it conveys the property. See *Puccetti v Girola* (1942) 20 C2d 574, 128 P2d 13. In that event, the grantor should be further identified by inserting the optional language provided in the form. Although there is no statute prohibiting or invalidating acquisitions or conveyances of real property made by an unqualified foreign corporation, such a corporation may be penalized for transacting intrastate business. Corp C §§2203(c), 2258.

Under *Snukal v Flightways Mfg., Inc.* (2000) 23 C4th 754, 98 CR2d 1, a conveyance signed by any two of the chairpersons of the board, the president or any vice president and the secretary, any assistant secretary, the chief financial officer, or any assistant treasurer of a corporation will not be invalidated for the corporation by lack of authority of the signing officers, as long as no third party dealing with those officers had actual knowledge that they had no authority to execute the conveyance. (See Corp C §313, the statute that the court was interpreting.) A conveyance executed by one person who holds two of the requisite capacities is binding. 23 C4th at 784.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.21 g. Form: Joint Venture

§10.21 g. Form: Joint Venture

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.15-10.21.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.21-1 Joint venture

_ _[*Names of joint venturers*]_ _**, constituting all the joint venturers in** _ _[*name of joint venture*]_ _**, a joint venture,**

Comment: For the most part, the designation "joint venture" should simply be avoided because of uncertainties surrounding the legal consequences of the designation. Both partnerships (see §§4.24, 10.17) and unincorporated associations (see §10.16) can hold and convey real property in their own names, and most joint ventures can be characterized as one of those entities.

If the joint venture format is used, conveyances to the joint venture should be in the names of the joint venturers, not in that of the joint venture, and the joint venture name should be used only for identification.

© The Regents of the University of California

§10.22 h. Other Grantor Clauses

For discussion of sales by administrators and executors, and a form for executor's deed, see 1 California Decedent Estate Practice §§13.14-13.60 (Cal CEB 1986). On legal requirements for deeds executed by guardians and conservators, see Prob C §§2109, 2111.

The name and official capacity of an officer acting under court order or authority (*e.g.,* sheriff, marshal, constable, court commissioner, receiver, or referee in partition) should be stated in a deed from that person. This type of deed often contains a reference to the proceedings authorizing the conveyance, but the recital is not essential.

In describing cities, some lawyers add "a municipal corporation of the State of California" or similar language; in describing counties, "a body corporate and politic" is sometimes seen. Nevertheless, it is sufficient to say "the City of Los Angeles, California" or "Contra Costa County, California."

© The Regents of the University of California

§10.23 3. Words of Conveyance

The operative words of conveyance used will generally establish the type of deed with all the legal consequences that flow from the characterization. For example, using the word "grant" will make the deed a grant deed (CC §1092) and will invoke the implied covenants that the grantor has not conveyed the same estate to anyone other than the grantee and that the property is free of encumbrances placed on it by the grantor (CC §1113). See §10.2. Using the words "assign," "remise, release, and quitclaim," or merely "quitclaim," will characterize the instrument as a quitclaim deed without any implied covenants concerning title or encumbrances. See §10.4.

If the buyer intends that warranties and covenants stated in the purchase and sale agreement (other than those implied in the deed as covenants) are to survive delivery of the deed, the agreement should provide for their survival or the deed should recite the covenants. See §4.109.

To "waive" or "renounce" title, or to say that it "shall go to" the buyer, does not pass title. *Davis v McGrew* (1889) 82 C 135, 23 P 41; see also *Litten v Warren* (1936) 11 CA2d 635, 54 P2d 39.

© The Regents of the University of California

4. Grantee

§10.24 a. Requirement of Capacity

To take title, a grantee must be one of the following:

- A natural person (see CC §671);
- A general partnership, a limited partnership, or a corporation (see §§10.17-10.18, 10.20); or
- An unincorporated association authorized by law to take title to real property (see §10.16).

See §§4.7, 4.14-4.18 on capacity to hold title to real property. See §4.18 and Pen C §§2600-2601 on prisoners' rights.

Infants and incompetent or insane persons are capable of taking title because the law presumes their acceptance of a beneficial conveyance (see §§4.15-4.16). *Estate of Yano* (1922) 188 C 645, 206 P 995; see *Estate of Kalt* (1940) 16 C2d 807, 813, 108 P2d 401. See §4.17 for a discussion of guardianship as a prerequisite for conveying property for persons under disability.

© The Regents of the University of California

§10.25 b. Requirement of Certainty

The grantee must be so named or designated that his or her identity is absolutely certain. This requirement can be met without naming the grantee if a means of identification can be inferred from the language of the deed.

EXAMPLE 1: A quitclaim of an easement to "the record owners of all lots in the tract described below, in severalty, on the same tenures as their respective interests appear of record at the time of recording this deed" might be sufficient. See CC §§681 (severalty), 761 (tenures of estates).

EXAMPLE 2: Identification of the grantees as the "heirs or devisees of *A*, deceased, subject to the administration of his estate" was upheld as sufficient in *Schade v Stewart* (1928) 205 C 658, 272 P 567.

Examples of deeds void for uncertainty are deeds to the following:

- "*A* or *B*." See *Schade v Stewart, supra* (dictum). See also §4.157 for discussion of the problems presented when the purchase and sale agreement requires the deed to recite the grantee as "*A* or nominee."
- "The inhabitants of the City of Los Angeles" (except for dedicating an easement for public use). See Comment, 14 Cal L Rev 135 (1926).
- A fictitious person (*Copeland v Fairview Land & Water Co.* (1913) 165 C 148, 162, 131 P 119); but a deed to an actual person under an assumed name is valid (*Wilson v White* (1890) 84 C 239, 24 P 114).

© The Regents of the University of California

§10.26 c. Status of Grantee

It is customary to show the marital status of a grantee and the marital relationship of grantees who are husband and wife. See Fam C §§700, 760, 803 on the community property presumption when a husband and wife are so described in a deed. Title insurers require that deeds describe the status of grantees to increase certainty of identification. See also §4.21.

Common status designations are: an unmarried man (or woman); husband and wife; a married woman (or man); his (or her) spouse; a minor; an incompetent person; and an administrator, trustee, or executor. A deed to a minor or incompetent person should run directly to that person rather than to the guardian or conservator, but deeds often name the guardian as grantee and add a recital of guardianship. A conveyance to heirs or devisees of the decedent can run either to the heirs or devisees or to the administrator or executor. However designated, it is customary to include a recital that the conveyance is subject to administration of the estate.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.27 d. Other Required Elements

§10.27 d. Other Required Elements

In addition to the name and status of the grantee or grantees, three other elements of the grant are necessary, if applicable:

- The nature of the estate (see §10.28);
- The nature of ownership (see §10.29); and
- The proportion of interest (see §10.30).

A single grant may entail questions concerning each of these elements. For example, "to the following as tenants in common: *A* and *B*, husband and wife, as joint tenants, an undivided one-half; *C* and *D*, husband and wife, as community property, an undivided one-third; and *E*, a married woman, as her separate property, an undivided one-sixth."

© The Regents of the University of California

§10.28 (1) Nature of Estate

If the nature of the estate is not otherwise stated, the deed is presumed to pass an estate in fee. CC §1105. Other kinds are estates for life, estates for years, and estates at will. See CC §761. The intent to pass an estate other than fee title must be expressed in the deed.

The grant should make clear whether the estate passed is one of full ownership (a fee) or one of more limited interest (such as an easement). See *Johnson v Ocean Shore R.R.* (1971) 16 CA3d 429, 94 CR 68. See also *Warren v Atchison, T. & S.F. Ry.* (1971) 19 CA3d 24, 96 CR 317. Estates may be divided into present and future interests.

© The Regents of the University of California

§10.29 (2) Nature of Ownership

Multiple ownership may be in joint tenancy, tenancy in common, community property, or partnership interests. CC §§682-687. All real property in California, and all personal property wherever located that is acquired during marriage, is community property (Fam C §§700, 760, 803), with some exceptions (Fam C §770). However, real or personal property acquired by a married woman by written instrument before January 1, 1975, is presumed to be her separate property. Fam C §803. The deed should express the buyers' wishes about the nature of ownership. On multiple ownership generally, see §§4.21-4.23.

© The Regents of the University of California

§10.30 (3) Proportion of Interest

A grant, for example, "to *A* and *B* as tenants in common" gives the grantees undivided equal shares. If two or more persons take as tenants in common under an instrument that is silent on their respective shares, a presumption arises that their shares are equal. *Caito v United Cal. Bank* (1978) 20 C3d 694, 705, 144 CR 751. The shares may be made unequal by an express provision in the deed or may be shown to be unequal by parol evidence. *Anderson v Broadwell* (1931) 119 CA 150, 6 P2d 267. To avoid litigation, the proportions should be expressed in the deed, even when equal, *e.g.,* by specifying "undivided equal shares."

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/ e. Grantee Recitals/§10.31 (1) Form: Joint Tenancy

e. Grantee Recitals

§10.31 (1) Form: Joint Tenancy

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.31-10.34.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.31-1 Joint tenancy

_ _[*Names of grantors*]_ _ _ _[*state words of conveyance*]_ _ **to** _ _[*names of grantees*]_ _ **as joint tenants.**

Comment: Because a joint tenancy conveyance is made to two or more people in equal shares (CC §683), the proportions of the respective interests need not be specified. See §10.30. The salient characteristic of joint tenancies, of course, is the right of survivorship in remaining joint tenants, which removes the property from the decedent's estate. CC §683; Prob C §223. Features of joint tenancies are discussed in §4.22.

A joint interest in property can be created by any of the following as grantor (CC §683):

- A sole owner to himself or herself and others (see *Estate of Bibb* (2001) 87 CA4th 461, 104 CR2d 415, regarding transmutation of a grantor's separate property interest into joint tenancy held by grantor and another);
- From tenants in common or joint tenants to (a) themselves or some of them and (b) themselves or any of them and others; or
- From husband and wife, when holding title as community property or otherwise, to (a) themselves, (b) themselves and others, or (c) one of them and to another or others.

© The Regents of the University of California

§10.32 (2) Form: Tenancy in Common

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.31-10.34.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.32-1 Tenancy in common

_ _[*Names of grantors*]_ _ _ _[*state words of conveyance*]_ _ **to** _ _[*names of grantees*]_ _ **an undivided** _ _[*e.g., one-half*]_ _ **interest and to** _ _[*names of grantees*]_ _ **an undivided** _ _[*e.g., one-third*]_ _ **interest,** _ _[*state any other interests*]_ _ **as tenants in common.**

Comment: Tenants in common may hold their interests in disproportionate shares (see CC §685), but if the shares are not specified, they will be presumed to be equal. See §4.22 on other features of tenancies in common.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.33 (3) Form: Community Property

§10.33 (3) Form: Community Property

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.31-10.34.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.33-1 Community property

_ _[*Names of grantors*]_ _ _ _[*state words of conveyance*]_ _ **to** _ _[*names*]_ _**, husband and wife, as their community property.**

Comment: A deed to grantees as husband and wife without a specification of the form of ownership is presumed to convey title as community property (Fam C §§760, 2580-2581), but this presumption may be overcome by clear written evidence of an agreement to the contrary. In cases not involving divorce or separation, tracing contributions to the purchase of the property back to separate property sources may also be admissible evidence to rebut the presumption. See Fam C §2640; *Marriage of Weaver* (2005) 127 CA4th 858, 865, 26 CR3d 121; *Marriage of Haines* (1995) 33 CA4th 277, 39 CR2d 673. See §4.21 on community property.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.34 (4) Form: Changing Title From Joint Tenancy to Community Property

§10.34 (4) Form: Changing Title From Joint Tenancy to Community Property

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.31-10.34.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.34-1 Changing title from joint tenancy to community property

_ _[*Names of husband and wife; see Comment below*]_ _ _ _[*words of conveyance*]_ _ **to** _ _[*names of husband and wife*]_ _**, husband and wife, as their community property,**

Comment: Although it is common practice for brokers and title companies to suggest that married couples who acquire real property take title as joint tenants, ownership in community property is preferable to joint tenancy for federal tax purposes. On the death of a joint tenant, one-half of the basis of the property is stepped up to the time of death (IRC §1014(b)(9)), but the entire basis is stepped up on the death of a spouse if the property is held as community property (IRC §1014(b)(6)). The parties could also execute an independent agreement that the property will be treated as community property if they do not wish to execute a new conveyance. See §10.33. A conveyance from husband and wife as joint tenants to themselves as their community property will not trigger a reappraisal of the property for property tax purposes under Cal Const art XIIIA. Rev & T C §63.

If the person recording this form claims an exemption from the documentary transfer tax, the county recorder's office will require that the document include a statement of authority for the exemption. The names used by husband and wife in filling in the grantor portion of the deed must be the same as they appear in the joint tenancy deed by which they took title.

© The Regents of the University of California

§10.35 5. Description

Real property can be transferred only by a writing that describes the property (*Craig v Zelian* (1902) 137 C 105, 69 P 853) with sufficient clarity that it can be identified and located (*Best v Wohlford* (1904) 144 C 733, 78 P 293; *Podd v Anderson* (1963) 215 CA2d 660, 30 CR 345). No particular form of description is required (see, *e.g.,* CC §1092) as long as the description permits identification of the property. If the description is omitted or not sufficiently certain, however, the conveyance is void. *Edwards v City of Santa Paula* (1956) 138 CA2d 375, 292 P2d 31.

The description generally follows directly the designation of the grantee. See, *e.g.,* the grant deed in §10.7. On descriptions generally, see chap 11.

"Subject to" clauses (see §10.37) and special recitals (see §§10.38-10.52) follow the description and may be inserted in the space for description if there is enough room. If not, it is generally better to type the entire deed than to attach an exhibit to a printed form.

© The Regents of the University of California

§10.36 6. Exhibits and Riders

If, for any reason, an exhibit is to be attached to the deed, recorders prefer that it be attached as a second page rather than pasted to the front of the deed and folded.

Some recorders take the position that a rider covering provisions other than the description is not "legible" and may require the person presenting it for record to prepare a substitute for the "illegible" original. Govt C §27361.7.

© The Regents of the University of California

§10.37 7. "Subject to" Clauses

Grant deeds are often restrained by conditions or qualifications, agreed on by grantor and grantee, that negate the grantor's liability under implied covenants. See CC §1113. These conditions or qualifications are the "subject to" clauses of grant deeds. For discussion of the restrained grant deed and for examples of "subject to" clauses, see §12.23. These clauses are not to be confused with contractual conditions commonly introduced by similar words.

© The Regents of the University of California

§10.38 8. Special Recitals

When appropriate, various special recitals should be incorporated in a deed to explain its purpose, show the interest and intent of the parties, and incorporate by reference other recorded documents. Some common recitals are presented as illustrations and discussed individually in §§10.39-10.52. Special recitals should be used liberally because they clarify the parties' intent and eliminate the effect of legal presumptions that may operate contrary to the parties' intentions (see, *e.g.,* CC §686 (presumption of tenancy in common); Fam C §§700, 760, 803 (presumption of community property)). On the conclusive presumption of recitals in written instruments, other than recitals of consideration, see Evid C §622.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.39 a. Form: Spouse-to-Spouse Recital of Separate Property

§10.39 a. Form: Spouse-to-Spouse Recital of Separate Property

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.39-10.52.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.39-1 Spouse-to-spouse recital of separate property

This deed is given to carry out the mutual desire and agreement of the parties that the property shall become vested in the grantee as _ _[*his/her*]_ _ sole and separate property.

Comment: Either spouse may enter into any property transaction with the other that either might if unmarried. Fam C §721. However, they should state their intentions explicitly. In a deed from one to the other, when the intent is to vest title in the grantee as his or her separate property, this form is a useful recital.

Despite the recital of vesting as separate property, either spouse can show against the other that there was no intention to change the property from community to separate. Compare *Salveter v Salveter* (1929) 206 C 657, 275 P 801, with *Donze v Donze* (1928) 88 CA 769, 264 P 294. If the wife is the grantee of an interest acquired before January 1, 1975, the presumption of separate property is conclusive in favor of a third party who deals with her in good faith and for value. Fam C §803. When the husband is the grantee and a third party deals with him in good faith and for value, the wife is estopped from denying the separate property recital in the deed. *MacKay v Darusmont* (1941) 46 CA2d 21, 115 P2d 221.

Some title companies require this recital in deeds between husband and wife as a condition to insuring title as separate property or to insuring a subsequent conveyance from the grantee spouse.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.40 b. Form: Consent to Joint Tenancy Between One Spouse and Another Person

§10.40 b. Form: Consent to Joint Tenancy Between One Spouse and Another Person

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.39-10.52.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.40-1 Consent to joint tenancy between one spouse and another person

_ _[*Name of grantee spouse*]_ _**, named above as a grantee, and** _ _[*name of consenting spouse*]_ _**,** _ _[*his wife/her husband*]_ _**, consent to the creation in the grantees of a joint tenancy in the property described in this deed.**

[*Execution and acknowledgment by consenting spouse*]

Comment: In *Yeoman v Sawyer* (1950) 99 CA2d 43, 221 P2d 225, a husband contributed half the purchase price of property from community funds and took title, without his wife's consent, under a joint tenancy deed with a single woman who contributed the other half of the purchase price. The court regarded the interests under the deed as being one-quarter vested in the husband, one-quarter in the wife (giving her half of the community property), and the other one-half in the single woman. Because the interests were unequal, the joint tenancy was defeated, and a tenancy in common was held to have been created.

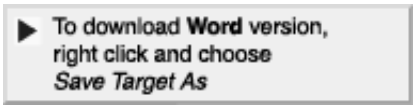
Before insuring title in grantees as joint tenants when one of the grantees is married, title companies, to remove doubt about the status of title to the property, require (1) a recital in the deed similar to the one presented above, (2) the consenting spouse's signature on the deed, and (3) acknowledgment of the recital. As an alternative, title insurers will accept as evidence of consent escrow instructions, signed by the consenting spouse, authorizing the joint tenancy. Having the consent in the deed is preferable, however, because off-record evidence may be unavailable, lost, or destroyed. On execution, see §§10.53-10.66. On acknowledgments, see §§10.67-10.70.

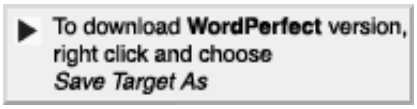
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.41 c. Form: Deed in Lieu of Foreclosure

§10.41 c. Form: Deed in Lieu of Foreclosure

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.39-10.52.





10.41-1 Deed in lieu of foreclosure

This deed is an absolute conveyance, grantor(s) having sold the property to grantee(s) for a fair and adequate consideration. The consideration is _ _[*the sum of* _ _[*dollar amount*]_ _ *and*]_ _ full satisfaction of all obligations secured by the _ _[*mortgage/deed of trust*]_ _ securing the obligation of _ _[*name*]_ _ in favor of _ _[*name*]_ _ recorded on _ _[*date*]_ _, as Instrument _ _ in book _ _, page _ _ of _ _[*official book*]_ _, in the Office of the County Recorder of _ _[*name*]_ _ County. This conveyance is freely and fairly made, and no agreements other than this deed have been made between grantor(s) and grantee(s) with respect to the property.

Comment: Civil Code §2889 declares that all contracts for the forfeiture of property subject to a lien in satisfaction of the obligation secured, as well as contracts in restraint of the right of redemption, are void. There are two major problems associated with a mortgagee's acceptance of a deed in lieu of foreclosure. The first problem is that there is no foreclosure sale to extinguish any junior liens or interests that have attached. On delivery of the deed in lieu of foreclosure, the mortgagee's security interest will merge with the deed and the mortgagee will receive title subject to undesired liens or clouds on the title. For this reason a current preliminary report on the title is essential and an endorsement to the mortgagee's title policy is recommended. At least one court has allowed a lender to reject a deed in lieu of foreclosure on the discovery of an undesired junior lien. *Brereton v Burton* (1938) 27 CA2d 464, 81 P2d 238.

The second problem involves the waiver of the debtor's well-established right to the notice, reinstatement, and redemption protections available under CC §§2924-2924*l* and CCP §726. Civil Code §2889 declares that all contracts for the forfeiture of property subject to a lien in satisfaction of the obligation secured by that property, as well as contracts in restraint of the right of redemption, are void.

It has long been the law in California that the right of redemption may not be waived in advance, at the time of origination of the loan. *Bradbury v Davenport* (1896) 114 C 593, 46 P 1062; CC §2953. A later deeding of the property by the mortgagor to the mortgagee and waiver of the right of redemption can be treated as an exception to this rule, but only under the following conditions (*Hamud v Hawthorne* (1959) 52 C2d 78, 83, 338 P2d 387):

- The original loan was documented in proper form by a note secured by a deed of trust;
- Default has occurred in payment;
- The parties enter into a separate, distinct, and subsequent contract with separate consideration; and
- The transaction is fair and honest.

Waivers of the equity of redemption are strictly scrutinized. *Bradbury v Davenport, supra*.

Use of a deed in lieu of foreclosure must therefore satisfy, at a minimum, the above criteria. In addition, it is essential that a title insurer be consulted in advance to determine whether the instrument will be insurable. Requirements of title insurers vary greatly, depending on the circumstances of the transaction. In instances involving individual debtors and single-family residences serving as security, a deed in lieu of foreclosure may be difficult to insure. In an arm's-length transaction involving sophisticated parties and commercial property, a title insurer may be able to satisfy itself that the risk can be safely underwritten. See also Stillman, *The Treatment in Bankruptcy of Deed in Lieu of Foreclosure Agreements*, 9 Cal Real Prop J 19 (Spring 1991).

In addition to the recitals in form 10.41-1, it may be appropriate to include recitals to the effect that the borrower desires to avoid the stigma of foreclosure, that the debt equals or exceeds the value of the security, that the parties have consulted with counsel of their choice, and that the waiver of the right of redemption is knowingly made on an

informed basis. If the borrower is to remain liable for a portion of the debt exceeding the value of the security, the circumstances should be clearly specified. Some title insurers will require a carefully drafted estoppel certificate; in certain circumstances, recitals may be placed in the deed, and some title insurers will require both.

See California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 7 (4th ed Cal CEB 2009) for discussion of deeds in lieu of foreclosure and title company practices in handling them.

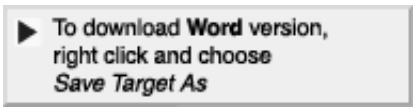
© The Regents of the University of California

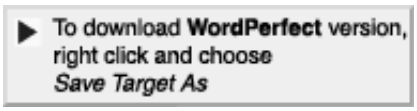
Source: Real Property/California Real Property Sales Transactions/10 Deeds/ d. Correcting, Removing, and Releasing Recitals/§10.42 (1) Form: Correcting or Clarifying Description of Property

d. Correcting, Removing, and Releasing Recitals

§10.42 (1) Form: Correcting or Clarifying Description of Property

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.39-10.52.





10.42-1 Correcting or clarifying description of property

This deed is given to _ _[*correct the erroneous/clarify the indefinite*]_ _ description of the property contained in the deed recorded on _ _[*date*]_ _, as Instrument _ _ in book _ _, page _ _ of _ _[*official book*]_ _, in the Office of the County Recorder of _ _[*name*]_ _ County, and is in lieu of that deed.

Comment: Erroneous descriptions in deeds fall into one of two categories:

- The description is sufficient despite the errors and will not void the deed, because the property intended to be conveyed can be ascertained (*Leonard v Osburn* (1915) 169 C 157, 146 P 530; *Rogers v McCartney* (1906) 3 CA 34, 84 P 215).
- The description is not sufficient, because the property intended to be conveyed cannot be ascertained. In this event, the deed can be voided. *Morehart v County of Santa Barbara* (1994) 7 C4th 725, 29 CR2d 804; *Davis v Ward* (1895) 109 C 186, 41 P 1010; *Saterstrom v Glick Bros. Sash Co*. (1931) 118 CA 379, 5 P2d 21.

A grant, subject to certain exceptions, is interpreted in favor of the grantee. CC §1069. To interpret the description in the grantee's favor, the court will reject what is apparently false in the description and uphold the deed if the remainder of the description is applicable to the property intended to be conveyed. See *Podd v Anderson* (1963) 215 CA2d 660, 30 CR 345. See §§11.89-11.93 on erroneous and indefinite descriptions. Despite the new deed, intervening interests may have priority unless the erroneous or unclear description can be upheld as sufficient.

The directive of CC §1069 that a grant by a public agency is to be interpreted in favor of the grantor applies only if the grant is ambiguous. *Red Mountain LLC v Fallbrook Pub. Util. Dist.* (2006) 143 CA4th 333, 344, 48 CR3d 875.

© The Regents of the University of California

§10.43 (2) Form: Removing Cloud on Title

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.39-10.52.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.43-1 Removing cloud on title

This deed is given to clear the records of any interest grantor may have in the property described in this deed because of any statement of any purported interest of grantor included by error in the deed recorded on _ _[*date*]_ _, as Instrument _ _ in book _ _, page _ _ of _ _[*official book*]_ _, in the Office of the County Recorder of _ _[*name*]_ _ County.

Comment: An erroneous conveyance of property not owned by the grantor creates a cloud on the title to that land. The title company will discover the cloud when the true owner orders a title search in connection with a contemplated sale or encumbrance. To obtain title insurance, the owner must remove the cloud.

The cloud can be eliminated by having the grantee execute a deed to the true owner. This document could be in the form of a quitclaim. The owner, however, may prefer a grant deed with its implied covenants (see §§12.5-12.7) that the grantee has not encumbered the property. If a grant deed is given, it should negate any implied covenants of title by including a recital like the one above.

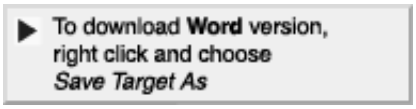
If the grantee is unwilling to execute and deliver a deed removing the cloud, the true owner should promptly commence an action to quiet title to remove the cloud, and file a lis pendens to cut off the rights of intervening third parties. See California Real Property Remedies and Damages, chap 7 (2d ed Cal CEB 2002).

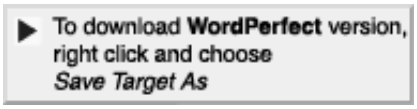
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.44 (3) Form: Release of Exception or Reservation

§10.44 (3) Form: Release of Exception or Reservation

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.39-10.52.





10.44-1 Release of exception or reservation of interest

This deed is given to relinquish and release all interest that the grantor may have in the property described in this deed because of any exceptions or reservations in the deed recorded on _ _[*date*]_ _, as Instrument _ _ in book _ _, page _ _ of _ _[*official book*]_ _, in the Office of the County Recorder of _ _[*name*]_ _ County.

Comment: A grant of real property passes a fee "unless it appears from the grant that a lesser estate was intended." CC §1105. The grant carries with it the following incidents and appurtenances unless they have been clearly excepted:

- A permanent building and its fixtures (*Fratt v Whittier* (1881) 58 C 126);
- Deposits, *i.e.,* minerals and other substances of the land (*Moore v Smaw* (1861) 17 C 199);
- Water rights necessary for the use of the land (*Stanislaus Water Co. v Bachman* (1908) 152 C 716, 93 P 858; for a discussion of appropriative water rights that are appurtenant and run with the land, see *Nicoll v Rudnick* (2008) 160 CA4th 550, 558, 72 CR3d 879);
- Rents not yet due from an existing lease on the land (*Fahrenbaker v E. Clemens Horst Co*. (1930) 209 C 7, 284 P 905);
- Award money from a pending condemnation proceeding (*Security Co. v Rice* (1932) 215 C 263, 9 P2d 817);
- Landowner's royalty from oil produced on the land (*Tanner v Title Ins. & Trust Co*. (1942) 20 C2d 814, 129 P2d 383);
- An easement for a road over adjoining lands that benefits the land conveyed (*Elliott v McCombs* (1941) 17 C2d 23, 109 P2d 329); and
- Title up to the center of an adjoining highway (CC §1112).

For general principles of law on the passing of incidents and appurtenances, see CC §§1084, 1104, 3522.

This form is commonly used to release incidents and appurtenances excepted from the original conveyance. It may also be used to eliminate problems created by thoughtless reiteration of reservations or exceptions in copying prior deeds. See §11.73 for discussion of reservations and exceptions; see §11.92 on reservations and exceptions in successive deeds.

© The Regents of the University of California

e. Compliance With Obligation Recitals

§10.45 (1) Form: Conveyance in Performance of Sales Agreement

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.39-10.52.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.45-1 Conveyance in performance of sales agreement

This deed is given in full satisfaction of an agreement to convey executed by grantor(s) to _ _[*assignor(s) of*]_ _ grantee(s), recorded on _ _[*date*]_ _, as Instrument _ _ in book _ _, page _ _ of _ _[*official book*]_ _, in the Office of the County Recorder of _ _[*name*]_ _ County.

Comment: This provision is designed to remove the lien of a purchaser under a recorded purchase agreement or installment land contract (CC §3050), and it may be used in a deed to either the buyer named in the agreement or the buyer's assignee.

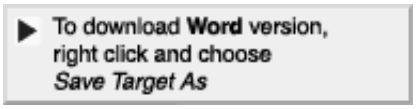
See Evid C §642 for the presumption that a person having a duty to convey real property actually conveyed when the presumption is necessary to perfect title.

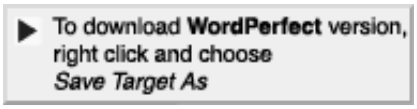
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.46 (2) Form: Conveyance on Exercise of Option

§10.46 (2) Form: Conveyance on Exercise of Option

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.39-10.52.





10.46-1 Conveyance on exercise of option

This deed is given and accepted in compliance with an option to purchase contained in a lease recorded on _ _[*date*]_ _, as Instrument _ _ in book _ _, page _ _ of _ _[*official book*]_ _, in the Office of the County Recorder of _ _[*name*]_ _ County, and as a cancellation of the lease and full release of all parties to the lease and their respective successors in interest, from all other obligations under the lease.

[*Execution and acknowledgment by grantee*]

Comment: Many leases include a provision permitting the tenant to purchase the property on the exercise of an option. Good practice requires that a lease containing an option be recorded. The lease must be acknowledged by the landlord as a condition to recordation. Govt C §27287. If the lease is not recorded, however, the tenant's possession of the property may be sufficient to put a buyer on notice of the tenant's option rights.

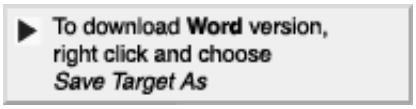
When the option is exercised, this provision should be used in the deed to evidence the intention of canceling the recorded lease. This form contemplates both an acceptance by the grantee and a general release between the parties. The grantee's signature must be acknowledged. For a detailed discussion of options, see chap 8.

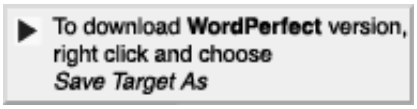
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.47 (3) Form: Conveyance on Distribution of Trust

§10.47 (3) Form: Conveyance on Distribution of Trust

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.39-10.52.





10.47-1 Conveyance on distribution of trust

The grantee having attained the age of majority, this deed is executed and delivered under the trust contained in the deed to the grantor recorded on _ _[*date*]_ _, as Instrument _ _ in book _ _, page _ _ of _ _[*official book*]_ _, in the Office of the County Recorder of _ _[*name*]_ _ County.

Comment: Probate Code §18100 protects a third person dealing with a trustee by, in effect, giving a third person who acts in good faith for valuable consideration, and without actual knowledge that the trustee is exceeding the trustee's powers or improperly exercising them, the status of a bona fide purchaser. Such third person is not bound to inquire whether the trustee has power to act or is properly exercising a power, and he or she may assume without inquiry the existence of a trust power and its proper exercise. Under §18100, if a good faith purchaser for value has no actual notice that the trustee was transferring the property in contravention of the terms of the trust, the purchaser would retain title to the property. This is apparently true even if the trustee converts the funds paid for the property by the good faith purchaser to his or her own use, because Prob C §18101 states that a third person who acts in good faith is not responsible for the trustee's proper application of trust property paid or delivered to the trustee.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/ f. Termination Recitals/§10.48 (1) Form: Termination of Recorded Lease

f. Termination Recitals

§10.48 (1) Form: Termination of Recorded Lease

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.39-10.52.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.48-1 Termination of recorded lease

This deed is given and accepted for the purpose of terminating the lease recorded on _ _[*date*]_ _, as Instrument _ _ in book _ _, page _ _ of _ _[*official book*]_ _, in the Office of the County Recorder of _ _[*name*]_ _ County.

[*Execution and acknowledgment by tenant*]

Comment: A lease creates both contractual and property rights in the tenant. *City of Pasadena v Porter* (1927) 201 C 381, 257 P 526. The lease may be terminated by surrender of the premises and unconditional acceptance by the landlord. *Flynn v Mikelian* (1962) 208 CA2d 305, 25 CR 138.

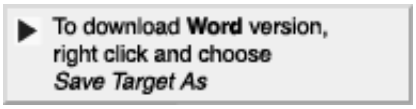
PRACTICE TIP: It is good practice to evidence the termination of a recorded lease—even if the lease itself reveals the termination—by a deed from the tenant to the landlord, containing this recital.

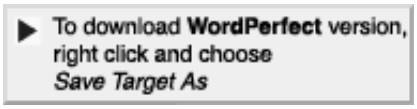
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.49 (2) Form: Elimination of Covenants, Conditions, and Restrictions

§10.49 (2) Form: Elimination of Covenants, Conditions, and Restrictions

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.39-10.52.





10.49-1 Elimination of covenants, conditions, and restrictions

This deed is given to cancel and annul all the covenants, conditions, restrictions, and reservations in the deed recorded on _ _[*date*]_ _, as Instrument _ _ in book _ _, page _ _ of _ _[*official book*]_ _, in the Office of the County Recorder of _ _[*name*]_ _ County, and to release the property described in this deed from any effect of all the above covenants, conditions, restrictions, and reservations.

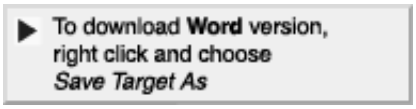
Comment: This provision is designed as a recital in a quitclaim deed given to eliminate covenants, conditions, and restrictions (CC&Rs). For discussion of CC&Rs, see §4.57. See also Advising California Common Interest Communities, chaps 6-7 (Cal CEB 2003).

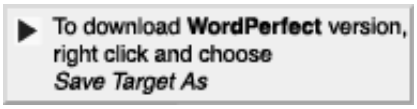
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.50 (3) Form: Removal of Power of Termination

§10.50 (3) Form: Removal of Power of Termination

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.39-10.52.





10.50-1 Removal of power of termination

This deed is given to convey all rights and powers to terminate the estate described in this deed, whether vested, conditional, or contingent, that grantor has now, or may acquire later because of the conditions, restrictions, or reservations in the deed recorded on _ _[*date*]_ _, as Instrument _ _ in book _ _, page _ _ of _ _[*official book*]_ _, in the Office of the County Recorder of _ _[*name*]_ _ County,

[*Add if relinquishment is only partial*]

but only to the extent _ _[*state rights relinquished, e.g., that they purport to establish setback lines from the front lines of the lots described in the recorded deed*]_ _. Except as above released, the conditions, restrictions, and reservations in the deed described above are to remain in full force and effect.

Comment: A grantor can impose a condition subsequent in a conveyance, which is a power to terminate the estate by appropriate action if there is a breach of the condition. *Boughton v Socony Mobil Oil Co*. (1964) 231 CA2d 188, 41 CR 714. The breach must be proved in an action to compel a reconveyance or quiet title. See *Parsons v Smilie* (1893) 97 C 647, 32 P 702.

The deed should be executed by the grantor who imposed the restrictions, or by his or her heirs, and it should be recorded.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/ g. Reservation Recitals/§10.51 (1) Form: Mineral Rights

g. Reservation Recitals

§10.51 (1) Form: Mineral Rights

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.39-10.52.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.51-1 Mineral rights

[*Insert after description of property conveyed; see §10.35*]

Reserving all oil, mineral, gas, and other hydrocarbon substances below a depth of 500 feet under the real property described in the deed, without the right of surface entry.

Comment: For discussion of reservations and exceptions, see §§11.73, 11.92. On the creation of easements, see §§11.104-11.107.

This provision is intended for a buyer who plans to use institutional financing to develop the property. Many institutional lenders will lend money on property when the borrower is not the owner of the mineral rights, if those rights are more than 500 feet below the surface and do not include the right of surface entry.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.52 (2) Form: Life Estate

§10.52 (2) Form: Life Estate

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.39-10.52.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.52-1 Life estate

Grantor reserves the exclusive possession and the use and enjoyment in _ _[*his/her*]_ _ own right of the rents, issues, and profits of the property described in this deed for the term of _ _[*his/her*]_ _ lifetime.

Comment: For discussion of reservations and exceptions, see §§11.73, 11.92. Elderly grantors often convey their property, reserving for their support a life estate in the rents, issues, and profits of the property. The recital in this section was upheld in *Tennant v John Tennant Memorial Home* (1914) 167 C 570, 140 P 242. The deed conveys to the grantee a future estate that, at the grantor's death, becomes an estate in possession. The conveyance is valid notwithstanding powers of revocation. *Belshe v Hope* (1995) 33 CA4th 161, 168, 38 CR2d 917. Reservation of a life estate can be coupled with a power of disposal. See *Estate of Wood* (1973) 32 CA3d 862, 875, 108 CR 522. Compliance with the requirements of any governing trust or instrument may be required under Prob C §§630-631.

Even though the owner of a life estate has the right to all rents, issues, and profits of the property during his or her lifetime (CC §818), when the life estate is created by a reservation in a conveyance of the fee, the right to the rents, issues, and profits should be expressly recited.

The owner of a life estate must keep the buildings and fences in repair and must pay taxes and other annual charges, an equitable proportion of special assessments (CC §840), and the interest on encumbrances (see *Boggs v Boggs* (1944) 63 CA2d 576, 147 P2d 116).

© The Regents of the University of California

D. Execution

§10.53 1. Date of Execution

A deed's validity is not affected by the lack of a date of execution or by an erroneous date. However, the date of execution may be evidence in determining priority among conflicting deeds, because a duly executed grant is presumed to have been delivered when executed. CC §1055. The presumption applies only to the time and not to the fact of delivery. *Blackburn v Drake* (1963) 211 CA2d 806, 27 CR 651. The date in the body of the deed gives rise to the presumption of §1055, although the presumption can be overcome by extrinsic evidence. *Gordon v City of San Diego* (1895) 108 C 264, 41 P 301. The presumption arises from the deed's date even if the date of acknowledgment is later. *Gordon v City of San Diego, supra*. An earlier acknowledgment date was held sufficient to overcome the presumption arising from the later date in *Merle v Meagher* (1870) 1 CU 644.

© The Regents of the University of California

§10.54 2. Definition

In a strict sense, execution consists of both the signing and delivery of an instrument. CCP §1933. The term "execution," however, is often used to mean only the signing of the instrument, as in CC §§1185, 1189-1190 (acknowledgment). See *Le Mesnager v Hamilton* (1894) 101 C 532, 35 P 1054. On delivery, see §§10.71-10.74.

© The Regents of the University of California

3. Requirements

§10.55 a. Who Signs

The deed must be signed by the grantor or the grantor's authorized agent. CC §1091. A deed not signed by the grantor is sufficiently executed if it is signed by a person in the grantor's presence, at the grantor's request, and with his or her authorization. *Knaugh v Baender* (1927) 84 CA 142, 257 P 606. The grantor may adopt and ratify his or her signature made by another without previous authority. *Blaisdell v Leach* (1894) 101 C 405, 35 P 1019. A deed signed by an interested person is subject to a rebuttable presumption that it is invalid. *Estate of Stephens* (2002) 28 C4th 665, 678, 122 CR2d 358.

The signature on the deed should conform exactly to the name shown as grantor. A deed signed and acknowledged by persons not named in the body of the deed as grantors does not pass their title. *Cordano v Wright* (1911) 159 C 610, 115 P 227. The rule in *Cordano* originated in the fact that common law deeds were not signed, but sealed, and identification of the grantor was therefore required in the body of the deed, but it is no longer given a mechanical application. *Strong v Strong* (1943) 22 C2d 540, 544, 140 P2d 386. If the name signed on the deed differs from the grantor's name, the conveyance is valid if the name in the acknowledgment conforms to the grantor's name in the body of the deed. *Middleton v Findla* (1864) 25 C 76.

For conveyances executed by corporations, see §10.20; for partnerships, see §10.17.

© The Regents of the University of California

§10.56 b. Spouse's Signature

Grantees and title insurers may require a spouse to join in the conveyance of the other spouse's separate property if they lack knowledge of the true character of the property. This can usually be accomplished through a quitclaim deed. Without a quitclaim deed, the accommodating spouse is exposed to potential personal liability for breach of covenants in the deed of conveyance. See *Evans v Faught* (1965) 231 CA2d 698, 711, 42 CR 133. See App M for suggested form of waiver to avoid the personal liability of the nonowning spouse. On implied covenants, see §§12.5-12.7.

Nevertheless, to avoid disputes and possible litigation, the parties must make sure that the signatures conform to the grantors named in the deed. On title company's requirements for establishing authority to act, see California Title Insurance Practice §2.34 (2d ed Cal CEB 1997).

© The Regents of the University of California

§10.57 c. Homestead Declaration

A homestead declaration under CCP §§704.910-704.995 does not restrict or limit any right of a spouse to convey or encumber the declared homestead. CCP §704.940. Each spouse, however, remains subject to the restrictions of Fam C §§752-754, 1102-1103, and 6321.

Spouses holding homesteaded property can unilaterally alter the form of ownership from joint tenancy to tenancy in common without affecting the homestead. *Estate of Grigsby* (1982) 134 CA3d 611, 618, 184 CR 886 (spouse severed joint tenancy by transfer to straw man, who then transferred property back).

© The Regents of the University of California

§10.58 d. Termination of Joint Tenancy

One joint tenant may sever a joint tenancy regarding his or her joint tenant interest, without consent of the other joint tenants, by doing the following (CC §683.2(a)):

- Deeding his or her joint tenant interest to a third person;
- Executing a written instrument with intent to sever (which includes a deed to transfer his or her joint tenant interest to himself or herself); or
- Declaring the severance in writing.

For more on the severance of a joint tenant interest, see CC §683.2.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/ 4. Particular Executions/§10.59 a. Form: Mark of Executing Party

4. Particular Executions

§10.59 a. Form: Mark of Executing Party

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.59-10.66.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.59-1 Mark of executing party

[*Mark of executing party*]

[*Name of executing party written by a witness*]

_ _[*Name of executing party*]_ _**, being unable to write, made** _ _[*his/her*]_ _ **mark in my presence and I signed** _ _[*his/her*]_ _ **name at** _ _[*his/her*]_ _ **request and in** _ _[*his/her*]_ _ **presence.**

Date: _ _ _ _ _ _

__[*Signature of witness*]__
_ _[*Typed name*]_ _

__[*Signature of additional witness*]__
_ _[*Typed name*]_ _

Comment: The mark of someone who cannot write has the same legal effect as a signature, as long as the name of the person making the mark is written near it by a person who writes his or her own name as a witness. If the signature is to be acknowledged, it must be witnessed by two persons, both of whom must subscribe their own names as witnesses. CC §14; Govt C §16.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.60 b. Form: Signature of Attorney-in-Fact

§10.60 b. Form: Signature of Attorney-in-Fact

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.59-10.66.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.60-1 Signature of attorney-in-fact

Date: _ _ _ _ _ _

__[*Attorney-in-fact signs executing party's name*]__,
_ _[*Typed name of executing party*]_ _

By: __[*Signature of attorney-in-fact*]__
Name: _ _[*Typed name*]_ _
Under power of attorney
dated _ _[*date*]_ _

Comment: Civil Code §1095 authorizes an attorney-in-fact to execute an instrument transferring an estate in real property if he or she subscribes the name of the principal to it and his or her own name as attorney-in-fact. "*A*, attorney-in-fact of *B*," does not satisfy §1095.

The importance of compliance with CC §1095 was discussed in *Hodge v Hodge* (1967) 257 CA2d 31, 64 CR 587, in which a deed executed by an authorized agent, who signed her principal's name and typed in her own name (as agent) but then failed to sign her own name, was declared invalid. The case contains a helpful review of previous California decisions on execution of deeds by an agent.

Civil Code §1091 requires that the power of attorney be in writing. Government Code §27322 permits the power of attorney to be recorded; most title insurance companies require its recordation. A recorded power of attorney affecting real property can be revoked only by recording the revocation in the same office in which the power of attorney was recorded. CC §1216. On revocation by death or incapacity, see CC §2356. For provisions of the Power of Attorney Law, see Prob C §§4000-4805. See also California Powers of Attorney and Health Care Directives (Cal CEB 2008).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.61 c. Form: Signature of Trustee

§10.61 c. Form: Signature of Trustee

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.59-10.66.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.61-1 Signature of trustee

Date: _ _ _ _ _ _ __[*Signature of trustee*]__
_ _[*Typed name*]_ _ **as trustee of** _ _[*name of trust*]_ _

Comment: Failure to indicate the representative capacity of the execution may be overcome by recitals in the deed or other record evidence indicating that the execution is actually in a representative capacity. For a form of recital for a trustee as grantor, see §10.19. Even when there is a representative capacity recital in the deed, failure to indicate that execution is made in that capacity can create problems. In *Estate of Conroy* (1907) 6 CA 741, 93 P 205, the deed named the grantor as "*A* (Administrator of the Estate of *B*)," and the deed was signed and acknowledged by *A*. The court disregarded the words in parentheses and held the deed to be that of *A*, individually.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.62 d. Form: Signature of Guardian or Conservator

§10.62 d. Form: Signature of Guardian or Conservator

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.59-10.66.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.62-1 Signature of guardian or conservator

Date: _ _ _ _ _ _

__[*Signature of* _ _[*guardian/conservator*]_ _]__
_ _[*Typed name*]_ _ **as** _ _[*guardian/conservator*]_ _ **of** _ _[*name of ward*]_ _**,**
_ _[*a minor/an incompetent person*]_ _

Comment: On guardians and conservators, see §10.22; on the consequences of failing to indicate that the execution was in a representative capacity, see §10.61.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.63 e. Form: Signature of Executor or Administrator

§10.63 e. Form: Signature of Executor or Administrator

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.59-10.66.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.63-1 Signature of executor or administrator

Date: _ _ _ _ _ _

__[*Signature*]__
_ _[*Typed name*]_ _ **as** _ _[*executor/administrator/ administrator with will annexed*]_ _ **of the** _ _[*will/estate*]_ _ **of** _ _[*name of decedent*]_ _**, deceased**

Comment: On the consequences of failing to indicate that the execution was in a representative capacity, see §10.61. For a form of executor's deed suitable for administrators and for administrators with the will annexed, see 1 California Decedent Estate Practice §13.60 (Cal CEB 1986).

Probate Code §7263 provides that a certified copy of the order confirming sale be recorded in the office of the county recorder of each county in which the land, or any part of it, lies.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.64 f. Form: Signature of Partner

§10.64 f. Form: Signature of Partner

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.59-10.66.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.64-1 Signature of partner

Date: _ _ _ _ _ _

_ _[*Name of partnership*]_ _,
a _ _[*state of organization*]_ _ **partnership**

By: __[*Signatures*]__
Name: _ _[*Typed names*]_ _
Its: _ _[*Titles*]_ _

Comment: In September 1996, California enacted the Uniform Partnership Act of 1994 (UPA) (Corp C §§16100-16962), which governs all general partnerships as of January 1, 1999. Corp C §16111. Corporations Code §16302 permits any partner to convey title to real property held in the partnership name. Under UPA, the Revised Limited Partnership Act (Corp C §§15611-15724), and the Uniform Limited Partnership Act of 2008 (Corp C §§15900-15912.07), any general partner (*i.e.,* any partner of a general partnership and only general partners—not limited partners—of a limited partnership) may convey title to real property that is held in the name of the partnership. Corp C §§16302(a)(1), 15643(a) (Corp C §15904.06(b)(2), operative Jan. 1, 2008, for new or electing limited partnerships).

The partnership is bound if the act of the general partner is apparently taken in the ordinary course of the partnership business, unless the general partner had no authority to act and the person with whom the general partner is dealing knew or had received notice that the general partner was not authorized to act. If an act is performed that is not apparently in the ordinary course of business, it binds the partnership only if the general partner was authorized to act. Corp C §§16301, 15643 (Corp C §15904.03, operative Jan. 1, 2008, for new or electing limited partnerships).

Corporations Code §16302(b) provides that the partnership may recover partnership property only if it proves that it was not bound under Corp C §16301 and can prove either of the following:

- The purchaser for value who acquired property held in the partnership name or in the name of partners, as partners, knew or had received notification that the person signing the transfer document was not authorized to bind the partnership; or
- The purchaser for value who acquired property held in the name of persons, without indication that the property was partnership property, knew or had received notification that the property was partnership property and that the person signing the transfer document lacked authority to bind the partnership.

Rather than subjecting the deed to the risk of attack, the grantee should insist that the deed be executed by all the partners. Alternatively, the partnership might authorize one or more partners to execute the deed under a resolution by all the partners or under the partnership agreement. Title insurers require that the statement of partnership authority (Corp C §16303) or a certificate of limited partnership (Corp C §15621 (Corp C §15902.01, operative Jan. 1, 2008, for new or electing limited partnerships)) be recorded.

A grant of authority to transfer real property held in the name of a partnership contained in a certified copy of a filed statement of partnership authority recorded in the office for recording transfers of that real property is conclusive in favor of a person who gives value without knowledge to the contrary, so long as a certified copy of a filed statement containing a limitation on that authority is not then of record. Corp C §§16105, 16303(d)(2). See *Federal Deposit Ins. Corp. v Superior Court* (1997) 54 CA4th 337, 346, 62 CR2d 713.

For more detailed discussion of partnerships, see §§4.24-4.26. See also Advising California Partnerships (3d ed Cal CEB 1999).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.65 g. Form: Signature of Corporate Officer

§10.65 g. Form: Signature of Corporate Officer

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.59-10.66.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.65-1 Signature of corporate officer

Date: _ _ _ _ _ _

_ _[*Name of corporation*]_ _,
a _ _[*state of incorporation*]_ _ **corporation**

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

Comment: The name of the corporation should appear in the signature, but corporate misnomers are not detrimental if the intended corporation's identity is clear. See *Sixth Dist. Agric. Ass'n v Wright* (1908) 154 C 119, 97 P 144.

Unless execution is acknowledged in accordance with CC §1189, title insurers require a certified copy of a resolution authorizing the conveyance. Some title insurers may waive the certified copy of the resolution in the following situations:

- A bank or a financial institution with a responsible reputation executes the instrument and the corporate act is routine and does not affect its own property; or
- The president or vice-president and secretary or assistant secretary execute the instrument on behalf of the corporation, the transaction is clearly within the ordinary scope of the business of the corporation, and the possible loss if execution is unauthorized would not exceed an amount the insurer feels is reasonable.

See Corp C §313. See also §4.28.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.66 h. Form: Signature of Joint Venturer

§10.66 h. Form: Signature of Joint Venturer

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§10.59-10.66.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

10.66-1 Signature of joint venturer

Date: _ _ _ _ _ _

__[*Signatures of joint venturers*]__
_ _[*Typed names*]_ _,
constituting all the joint venturers in _ _[*name of joint venture*]_ _**, a joint venture**

Comment: For discussion of joint ventures, see §10.21. Consistent with the practice recommended in §10.21 (*i.e.,* that conveyances to joint ventures be avoided but, if made, be in the names of the joint venturers, not in the name of the joint venture, and that the joint venture name need not be used except for identification), the execution form provides for the individual joint venturers to execute the deed. Although the joint venture is referred to, it is only for identification and is not required.

If the deed to the joint venture is in the form "to *X*, a joint venture, composed of *A*, *B*, and *C*," or "to *X*, a joint venture, and *ABC*," title insurers may require a deed from the joint venture executed by all the joint venturers and the joint venture, even though it may not be a legal entity capable of taking title.

The provision in §10.64 (partnership) or §10.65 (corporation) must be included in the provision in this section if any of the joint venturers is a partnership or a corporation.

The title company should be consulted on whether the spouses of the joint venturers must sign.

© The Regents of the University of California

E. Acknowledgment

§10.67 1. Legal Requirements

Unless excepted by statute, a document's execution must be either acknowledged or proved, and the acknowledgment or proof certified, before it can be recorded. Govt C §§27287-27288. On procedures for proving unacknowledged documents, see §10.70. An acknowledgment is a statement that the person who appears to have signed the document did in fact sign it (see, *e.g.,* CC §1189); it must be distinguished from a verification, which is a sworn statement that a document's contents are true (see CCP §446).

PRACTICE TIP: Blank acknowledgment forms can readily be obtained from most title companies and stationery stores. These forms (sometimes called wafers) need only be filled out and stapled to the document to be recorded. Acknowledgments can be made before a number of specified public officials (CC §§1181-1182), but the most common practice is to have a notary public execute the acknowledgment.

Civil Code §§1189-1190 specify a single statutory form of acknowledgment to be used in all situations.

PRACTICE TIP: The California Legislature amended laws relating to notaries and notarization of documents, which take effect January 1, 2008. One change, which affects everyone who uses a notary or seeks to record a document with a recorder's office in California, alters the required wording of the statutory form of acknowledgement. County recorders are likely to reject any document submitted for recording that does not have the new wording. See CC §1189.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.68 2. Documents That Need Not Be Acknowledged

§10.68 2. Documents That Need Not Be Acknowledged

The following documents may be recorded without being acknowledged or proved:

- Judgments affecting real property (Govt C §27282(a)(1));
- Certain certificates, extensions, and releases related to taxes (Govt C §27282(a)(4));
- Certain documents relating to mining claims and leases (Govt C §§27282(a)(3), 27283-27285; CC §1219);
- Letters patent, certain documents related to letters patent, mineral leases in which the United States is the lessor, certain copies of interdepartmental communications of the Department of the Interior, and certain copies of documents filed with the General Land Office (Govt C §§27285-27286);
- Fictitious mortgages or deeds of trust (CC §2952; Com C §9401);
- Lis pendens (no requirement in CCP §405.21, the enabling statute);
- Duplicate certificates of sale of real property sold under execution or under a court order (*Foorman v Wallace* (1888) 75 C 552, 17 P 680);
- Federal tax liens (Govt C §27330); and
- Notices of lien for postponed property taxes (Govt C §27282(a)(5)).

© The Regents of the University of California

§10.69 3. Effect of Acknowledgment

A certificate of acknowledgment is prima facie evidence of the execution of the document to which it is attached. Evid C §1451. A person who properly acknowledges that he or she has executed an instrument cannot deny execution against subsequent innocent parties after the certificate of acknowledgment is attached to the instrument. This is true even if he or she did not freely execute the document. *Bryan v Ramirez* (1857) 8 C 461. But see *Mentry v Broadway Bank & Trust Co*. (1912) 20 CA 388, 129 P 470 (rule inapplicable to encumbrance such as a mortgage).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.70 4. Proof of Unacknowledged Documents

§10.70 4. Proof of Unacknowledged Documents

An unacknowledged document that does not come under any of the exceptions listed in §10.68 may still be recorded if it is proved by one of the following:

- A party executing the document or a subscribing witness (CC §1195(a));
- Proof of handwriting under certain circumstances (CC §§1195, 1198); or
- Court action (CC §§1203-1204).

NOTE: Constructive notice of a defectively acknowledged instrument is imparted 1 year after recordation under CC §1207.

© The Regents of the University of California

§10.71 F. Delivery

A basic requirement for validity of a deed is its delivery. CC §1054; *Hudemann v Dodson* (1932) 215 C 3, 7 P2d 997. It is delivery that passes title. *Pellissier v Title Guar. & Trust Co*. (1929) 208 C 172, 280 P 947. Besides physical transfer of the deed and acceptance by the grantee, the grantor must intend to pass title for delivery to be complete. *Henneberry v Henneberry* (1958) 164 CA2d 125, 330 P2d 250. The grantor's intent is a question of fact to be determined from all the circumstances surrounding the transaction. *Blackburn v Drake* (1963) 211 CA2d 806, 27 CR 651.

On the right to waive ineffective delivery, see *Kish v Bay Counties Title Guar. Co*. (1967) 254 CA2d 725, 729, 62 CR 494.

© The Regents of the University of California

§10.72 1. Unconditional Delivery Is Required

Delivery to the grantee or the grantee's agent cannot be conditional if the grantor intended to pass title. CC §1056.

EXAMPLE 1: If the grantor intended to pass title but delivers the deed to the grantee on the condition that the grantee execute an agreement to pay money, or that the conveyance take effect only in the event of the grantor's death, delivery is absolute, and title passes immediately to the grantee. *Bias v Reed* (1914) 169 C 33, 44, 145 P 516; *Estate of Pieper* (1964) 224 CA2d 670, 687, 37 CR 46.

EXAMPLE 2: If the grantor believes, even though erroneously, that the condition is necessary for the deed to be effective, the delivery may fail for lack of the required intention, *i.e.,* there may be no delivery despite the physical transfer of the documents. *Hotaling v Hotaling* (1924) 193 C 368, 224 P 455.

To convey property subject to a condition effectively, the grantor should deliver the deed to a third party (*e.g.,* an escrow holder) who is not solely the grantee's agent. See CC §1057. On the use of an escrow to convey property subject to conditions, see chap 15.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.73 2. Rebuttable Presumptions on Delivery

§10.73 2. Rebuttable Presumptions on Delivery

There are a few rebuttable presumptions affecting the burden of producing evidence on the issue of delivery. The following are three of them:

- When the deed is in the grantee's possession, delivery is presumed. See *Podd v Anderson* (1963) 215 CA2d 660, 30 CR 345.
- When the deed is in the grantor's possession, nondelivery is presumed. *Miller v Jansen* (1943) 21 C2d 473, 132 P2d 801.
- Recordation of a deed at the grantor's request is prima facie proof of delivery with the grantor's intention to convey title. *Osterberg v Osterberg* (1945) 68 CA2d 254, 156 P2d 46.

If a recorded deed is found in the grantor's possession, however, there is a conflict of presumptions. *Hill v Donnelly* (1941) 43 CA2d 47, 110 P2d 135 (presumption of delivery created by recordation versus presumption of nondelivery by grantor's continued possession of deed).

© The Regents of the University of California

§10.74 3. Constructive Delivery

Delivery can be constructive if

- by agreement of the parties at the time of execution, it is understood that the deed is to be delivered, and the grantee is entitled to immediate delivery; or
- the deed is delivered to a stranger for the benefit of the grantee, and the grantee's assent is shown or may be presumed. CC §1059.

© The Regents of the University of California

§10.75 G. Acceptance

For a deed to be effective, it must be accepted by the grantee. See *Green v Skinner* (1921) 185 C 435, 197 P 60. If the grantee has knowledge of the beneficial grant, acceptance is presumed (see *Boye v Boerner* (1940) 38 CA2d 567, 101 P2d 757); if the grant is beneficial, the grantee's acceptance is presumed (*Kropp v Sterling Sav. & Loan Ass'n* (1970) 9 CA3d 1033, 88 CR 878). Knowledge as well as acceptance is presumed unless lack of knowledge is clearly proved. See *Marshall v Marshall* (1956) 140 CA2d 475, 479, 295 P2d 131; *Steitz v Irwin* (1949) 94 CA2d 871, 211 P2d 919; *Herman v Mortensen* (1945) 72 CA2d 413, 164 P2d 551. On the presumption of acceptance by minors and incompetent or insane persons, see §10.24. When the grantee is a corporation, its intention to accept can be shown by its acts or words (*e.g.,* acts of ownership generally, retention of the deed, execution of a mortgage). See *Canal Oil Co. v National Oil Co*. (1937) 19 CA2d 524, 66 P2d 197.

© The Regents of the University of California

III. VALIDITY OF DEEDS

§10.76 A. Void Deeds

A deed is void in the following cases:

- The grantor is a person judicially declared incompetent. CC §40. See §4.16.
- The grantor is a minor. Fam C §6701. See §4.15.
- The deed is executed in blank with the grantee's name later inserted without the grantor's authorization. *Trout v Taylor* (1934) 220 C 652, 32 P2d 968.
- The deed is undelivered, such as one stolen from the grantor or delivered by an escrow holder in violation of the grantor's instructions. *Hildebrand v Beck* (1925) 196 C 141, 236 P 301; *Gould v Wise* (1893) 97 C 532, 32 P 576.
- The deed contains uncertain language, *e.g.,* "*A* or *B*" (see §10.25). See *Schade v Stewart* (1928) 205 C 658, 272 P 567. On the use of "*A* or nominee" language, see §4.157.
- The deed is testamentary (*i.e.*, one expressly intended to operate on the death of the grantor or in contemplation of death) *unless* it is either executed with the formalities required of wills (*Van Core v Bodner* (1947) 77 CA2d 842, 176 P2d 784) or delivered on a condition to a third party (CC §1057).
- The deed is materially altered. *Jay v Dollarhide* (1970) 3 CA3d 1001, 84 CR 538.
- The deed is in excess of governmental authority. *L&B Real Estate v Housing Auth. of County of Los Angeles* (2007) 149 CA4th 950, 956, 57 CR3d 298 (deed of county property sold for nonpayment of taxes is void).
- The instrument violates the Subdivision Map Act, Govt C §66410-66499.37; *Sixells, LLC v Cannery Bus. Park* (2008) 170 CA4th 648, 652, 88 CR3d 235.

Void deeds do not pass title even in favor of innocent purchasers unless estoppel is present. See *Blaisdell v Leach* (1894) 101 C 405, 35 P 1019; *Crittenden v McCloud* (1951) 106 CA2d 42, 234 P2d 642.

A deed that is validly executed and delivered to the intended grantee but which is thereafter altered or forged to add additional names as grantees may be valid as to the intended grantee but is void as to all alterations subsequently added. *Lee v Lee* (2009) 175 CA4th 1553, 1558, 97 CR3d 516.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/10 Deeds/§10.77 B. Voidable Deeds

§10.77 B. Voidable Deeds

Examples of voidable deeds include the following:

- A fraudulently procured deed (*Seeger v Odell* (1941) 18 C2d 409, 115 P2d 977);
- A deed containing a mistake about the quantity of land conveyed (see *Danielson v Neal* (1913) 164 C 748, 130 P 716);
- A deed procured by undue influence (*Cox v Schnerr* (1916) 172 C 371, 156 P 509);
- A deed procured by duress or menace (*Campbell v Genshlea* (1919) 180 C 213, 180 P 336); and
- A deed from a grantor of unsound mind whose incapacity has not been judicially determined (*Hughes v Grandy* (1947) 78 CA2d 555, 177 P2d 939).

If the deed is voidable, a bona fide purchaser from the grantee obtains good title as against the grantor. *Duff v Randall* (1897) 116 C 226, 48 P 66.

© The Regents of the University of California

11

Descriptions of Property

Scott A. Sommer

I. INTRODUCTION
- A. Historical Background §11.1
- B. Nature and Purpose of Descriptions §11.2
- C. The Lawyer's Function
  - 1. Review of Legal Description §11.3
  - 2. Zoning and Subdivision Considerations §11.4
  - 3. Forms of Ownership §11.5
  - 4. Creation of Easements §11.6
  - 5. Common Interest Developments §11.7
- D. Limitations on Lawyer's Function §11.8

II. FINDING CORRECT DESCRIPTIONS
- A. Deeds §11.9
- B. Preliminary Report or Title Insurance Policy §11.10
- C. Inspection of Premises §11.11
- D. Surveys and Engineering Studies §11.12
- E. Title Services §11.13

III. READING DESCRIPTIONS
- A. Certainty Requirement §11.14
- B. Ambiguity §11.15
- C. Acreage Problems §11.16
- D. Reference to Government Surveys §11.17
  - 1. Base and Meridian §11.18
  - 2. Range and Township §11.19
  - 3. Section §11.20
  - 4. Quarters §11.21
- E. California Surveying Systems
  - 1. California Coordinate System of 1927 §11.22
  - 2. Alternative Surveying and Mapping Systems §11.23
- F. Subdivision or Parcel Maps §11.24
- G. Reference to Other Recorded Instruments §11.25
- H. Metes and Bounds Descriptions §11.26
  - 1. Natural Monuments §11.27
  - 2. Artificial Monuments §11.28
  - 3. Adjoining Lands §11.29
  - 4. Streets and Public Rights-of-Way §11.30
  - 5. Railroad Rights-of-Way §11.31
  - 6. Courses and Distances
    - a. Bearings and Degrees §11.32
    - b. General Courses §11.33
    - c. Curves §11.34
    - d. Use of Symbols and Written Descriptions §11.35
    - e. Monuments §11.36
    - f. Measurements §11.37
  - 7. Quasi Metes and Bounds §11.38
  - 8. Designation of North §11.39
- I. Lot Division Description §11.40
- J. General or Common Description §11.41

IV. MATTERS ALTERING OR AFFECTING DESCRIPTIONS
- A. Effect on Record Title §11.42
- B. Easements

1. Benefit and Burden §11.43
2. Rules of Construction and Interpretation §11.44
a. Limitation to Use of Specified Width §11.45
b. Right to the Use of Streets and Alleys Reflected on Subdivision Map §11.46
c. Inclusion of Rights for Utilities §11.47
d. Doctrine of Practical Location and Amendment of Written Descriptions by Actual Location §11.48
e. Interpretation by Language of the Document and Extrinsic Evidence §11.49
f. Accommodation of Future Needs §11.50
g. Exercise of General Grant of Easement in a Particular Course or Manner §11.51
h. Exclusivity of Easements §11.52
3. Off-Record Easements §11.53
a. Easements by Implication §11.54
b. Easements by Implied Reservation §11.55
c. Easement of Necessity §11.56
d. Easement by Prescription §11.57
4. Termination of Easements §11.58
a. Termination by Merger §11.59
b. Termination by Destruction of Servient Tenement §11.60
c. Termination by Incompatible Use or Misuse §11.61
d. Termination by Abandonment §11.62
e. Termination by Nonuse of Easements Acquired by Prescription §11.63
f. Termination by Adverse Possession §11.64
5. Identification of Dominant Tenement §11.65
6. Change in Burden on Servient Tenement §11.66
7. Appurtenant or in Gross §11.67
a. Distinguishing Characteristics §11.68
b. Transferability §11.69
8. Ambiguous Description §11.70
9. Uncertain Duration §11.71
10. Failure to Designate as Easement §11.72
11. Exception or Reservation §11.73
12. Failure to State All Purposes and Limitations §11.74
13. Precautions for Buyers §11.75
14. Precautions for Sellers §11.76
15. Adverse Possession, Prescription, and Implied Dedication §11.77
C. Doctrines of Agreed Boundaries and of Practical Location
1. Doctrine of Agreed Boundaries §11.78
2. Doctrine of Practical Location §11.79
D. Abandonment and Vacation §11.80
E. Effect of Water on Land §11.81
1. High-Water Mark, Low-Water Mark §11.82
2. Thread or Middle of Lake or Stream §11.83
3. Islands §11.84
4. Formerly Navigable Waters §11.85
5. Avulsion §11.86
F. Eminent Domain §11.87
G. Merger of Parcels §11.87A
H. Estoppel §11.88

V. ELIMINATING DEFECTS IN DESCRIPTIONS
A. Solutions to Typical Problems
1. Overlapping Descriptions §11.89
2. Failure to Close Metes and Bounds Description §11.90
3. Incomplete, Confusing, or Erroneous Descriptions §11.91
4. Reservation or Exception in Successive Descriptions §11.92
5. Fraudulent or Erroneous Surveys §11.93
B. Drafting to Eliminate Defects
1. Drafting Principles §11.94
a. Avoid Nonessential Language §11.95
b. Avoid Ambiguity §11.96
c. Use Precise Language §11.97
d. Know Statutory Rules of Construction §11.98
2. Drafting Particular Descriptions §11.99
3. Form: Description by Reference to Subdivision Map §11.100
4. Form: Description by Reference to Rectangular Survey Map §11.101

5. Form: Description by Reference to Deed or Other Instrument §11.102
6. Description by Metes and Bounds §11.103
C. Easements §11.104
1. Form: Reservation of Easement in Grantor §11.105
2. Form: Transfer of Appurtenant Easement §11.106
3. Form: Creation of Easement §11.107
4. Release of Easement §11.108
D. Describing Multiple Parcels §11.109
E. Eliminating Water Problems §11.110
F. Contract Provision for Expressing Covenants in Deed §11.111
G. Statutory Remedies
1. Quiet Title §11.112
2. Declaratory Relief §11.113
3. Good Faith Improver §11.114
4. Marketable Record Title §11.115
5. Expired Offers of Dedication §11.116
6. Destroyed Land Records §11.117

VI. DESCRIBING PERSONAL PROPERTY §11.118

© The Regents of the University of California

I. INTRODUCTION

§11.1 A. Historical Background

Real estate practitioners in California encounter a broad variety of legal descriptions of real property, both in origin and in the quality and precision of the description. Historically, chains of title generally originate from these sources:

- Rancho grants and existing titles from the Spanish government and Mexican governors in the years before 1846, to the extent recognized by the United States Land Commissions of the 1850s and the federal courts; and
- Grants from the public domain by federal patent, including mining and homestead claims, Indian lands, and railroad grants.

Lawyers often encounter later-generation descriptions that derive from these original sources. Land subdivision companies operated briskly in California from the 1870s onward, and legal descriptions containing or based on these original descriptions are commonly encountered. For a readable history of the initial division of California, see Robinson, Land in California (1979). The practices of the early subdividers of Los Angeles County, for example, are described in Jackson, The Crabgrass Frontier: The Suburbanization of the United States (1985).

The quality of the early descriptions and first-generation subdivisions varied enormously. Early measurement techniques lacked precision, and, in any event, many of the described monuments are now gone. Early surveyors of townships and subdivisions in the late 1800s typically drew maps lacking some or all courses and monuments, even in urban areas. Many grants by federal patents used distant monumentation from the base line system. See §§11.17-11.18. Varying degrees of attention were paid to access easements and other necessary appurtenances.

PRACTICE TIP: Precision in land descriptions is relative. Even today, although parcel maps and legal descriptions that are derived from permanent monuments and prepared with modern techniques eliminate many problems, discrepancies in measurement or interpretation can still occur.

In light of this background, a number of corrective doctrines apply to the interpretation and use of legal descriptions:

- Unmentioned appurtenances (CC §§1084, 1104; see §§11.54-11.55);
- The doctrines of agreed boundaries and practical location (see §§11.78-11.79);
- Way of necessity (see §11.56);
- Adverse possession (CCP §§321-325; see §11.77); and
- Other off-record modifications of recorded descriptions.

These factors should always be kept in mind by parties considering the acquisition, transfer, or subdivision of land, or the acquisition and interpretation of title insurance products.

© The Regents of the University of California

§11.2 B. Nature and Purpose of Descriptions

The purpose of a description depends on the objective of the legal document involved. For example, purchase and sale agreements—even those involving large-scale commercial property—commonly refer to a street address, an assessor's parcel number, or other common reference, with additional provisions subjecting the property's full legal description and its insurability to the buyer's review and approval. For purposes of an instrument transferring title, such as a deed or a deed of trust, common descriptions are inadequate, and most title insurers will insure only the legal descriptions, as described in §§11.24-11.26. Using and accepting a legal description usually means accepting a small risk that the actual lines of possession differ from the metes and bounds of record, or that other doctrines or remedies may apply (see §§11.54-11.57, 11.77-11.79).

PRACTICE TIP: The best descriptions are produced or confirmed by modern survey techniques and insured by American Land Title Association (ALTA) policies of insurance for owners or lenders. On ALTA surveys, see California Title Insurance Practice §4.32 (2d ed Cal CEB 1997).

Regardless of the instrument or use involved, a description is intended to specifically delineate the property with a sufficient degree of precision that it can be located and distinguished from all other parcels, and that buyers, lenders, and title insurers will accept it as marketable. Lack of precision may result in expense, litigation, or disruption of commercial real estate transactions. On descriptions generally, see 12 Witkin, Summary of California Law, *Real Property* §271 (10th ed 2005); 3 Miller & Starr, California Real Estate §§8:45-8:51 (3d ed 2000).

On describing personal property incidental to transfers of real property, see §11.118.

© The Regents of the University of California

C. The Lawyer's Function

§11.3 1. Review of Legal Description

It is important for the attorney to review the legal description in any transaction to ascertain the type of description involved, its degree of precision, any issues that may arise when title insurance is requested, and whether it completely describes all property interests contemplated in the transaction. Counsel may also find it appropriate to refer the client to a surveyor or to explain the different types of title insurance that may be available to match the client's objectives, and the potential exceptions to coverage. Many circumstances may require a different description from the one by which the transferor acquired title:

- The original description may be erroneous (see §11.9);
- Subsequent events may have either deprived the record owner of all or part of the land or enlarged the transferor's holdings (see §§11.77-11.79);
- The record itself may reveal changes in the client's ownership (see §11.7); or
- The transferor may wish to part with only a portion of the land described in the documents (see §11.40).

To meet these situations, the lawyer—whether counsel for buyer or seller—must know how to find correct descriptions (see §§11.9-11.13), read them (see §§11.14-11.41), verify their accuracy (see §§11.42-11.88), correct them if necessary, and draft descriptions that will carry out the parties' intentions (see §§11.89-11.108), or refer the client to specialists, such as licensed surveyors or title companies, who will perform these functions.

In addition, the lawyer must know how to describe any personal property that is to be transferred as part of the transaction. On descriptions of personal property, see §11.118.

© The Regents of the University of California

§11.4 2. Zoning and Subdivision Considerations

An immediate concern in an acquisition may be a client's plans for future use, development, or subdivision of the property. If a client has calculated an economic return on the basis of development or subdivision of the property, it is important to point out that an inaccurate description may result in a shortfall in land, affecting densities or setbacks under local zoning ordinances.

If easements will be needed for access to a development, the client must be cautioned that public works and zoning considerations may apply to easement widths and designs. On development easements, see California Easements and Boundaries: Law and Litigation, chap 2 (Cal CEB 2008).

EXAMPLE: If a client has created a tentative map with minimum lot sizes and issues arise concerning boundary inaccuracies, the client's plans could be seriously disrupted. The lawyer should therefore counsel the client to condition the acquisition of property on careful inspection, a survey, and issuance of the appropriate form of title insurance.

© The Regents of the University of California

§11.5 3. Forms of Ownership

Many aspects of the transaction involving descriptions are exclusively the province of the lawyer. Foremost is the nature of the estate and form of ownership, such as a fee title, life estate, estate for years, leasehold, or separate versus community property or other form of cotenancy. The form of conveyancing and ownership, and use of a grant with covenants of title under CC §1113, are also the province of the lawyer. Title insurers will examine the description and form of title to determine whether they will insure the title as requested; however, the determination of the type of ownership or estate is a matter of counseling between the lawyer and the client. The lawyer should review the form of documents, even if prepared by an escrow holder or a title insurer, to make sure that they are consistent with the form of recommended ownership and that the form of title insurance used is consistent with these objectives.

© The Regents of the University of California

§11.6 4. Creation of Easements

The lawyer responsible for drafting an easement must make sure that the conveyance is properly drafted and consistent with record ownership, that it appropriately states the parcel to which it is appurtenant, and that issues of common use, ownership, maintenance (see CC §845), and compliance with applicable zoning codes are addressed. If an easement in gross is intended (see §11.67), the status and transferability of the easement must be properly created. For the description itself, the lawyer will refer the client to a surveyor for the metes and bounds or other description to be included in the conveyance, but the other aspects of the transaction require legal skills. On creation of easements, see California Easements and Boundaries: Law and Litigation, chap 1 (Cal CEB 2008).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/11 Descriptions of Property/§11.7 5. Common Interest Developments

§11.7 5. Common Interest Developments

Common interest developments are sophisticated combinations of privately and commonly held interests, for which the attorney must request and use descriptions of various types, but the structure of ownership, the creation of common areas, the duties of maintenance, and compliance with applicable laws and regulations are legal functions.

Descriptions will be employed in the drafting of restrictions on use or equitable servitudes for the creation of common interest developments. To be enforceable, restrictions require the following (CC §1468):

- A statement that successive owners in the land are bound by the restrictions;
- A proper definition of the acts related to the use of the land;
- A description of the land to be burdened by the covenants;
- A description of the land to be benefited; and
- Proper recording of the instrument containing the covenants (the declaration of restrictions, commonly called "covenants, conditions, and restrictions" or "CC&Rs") in the office of the recorder of each county in which such land or some part of it is situated.

Prior recorded CC&Rs bind the lots encumbered by the CC&Rs, even though the deeds to the encumbered lots do not reference the CC&Rs, see *Citizens for Covenant Compliance v Anderson* (1995) 12 C4th 345, 47 CR2d 898, and even though sellers failed to disclose the deed restrictions, see *Alfaro v Community Housing Improvement Sys. & Planning Ass'n* (2009) 171 CA4th 1356, 1372, 89 CR3d 659.

Counsel must make sure that the conveyances and the CC&Rs are appropriately drafted and indexed at the recorder's office so that subsequent parties dealing with the property will be on constructive notice of the conveyance. The lawyer cannot merely assume that these steps will be checked by a title insurer, even when title insurance is requested and issued.

See Forming California Common Interest Developments, chap 7 (Cal CEB 2004); Advising California Common Interest Communities §§7.44-7.53 (Cal CEB 2003).

© The Regents of the University of California

§11.8 D. Limitations on Lawyer's Function

The lawyer's responsibilities regarding descriptions will usually be discharged by recommending and using appropriate experts. Sections 11.12-11.13 examine several situations in which surveyors, engineers, and title insurers should be employed.

The lawyer should not be held to a standard of care in which responsibility for an error of a different professional will be attributed to the lawyer, unless the error is so obvious that it should be uncovered during the lawyer's examination.

Once the lawyer has employed the proper assistance, he or she should:

- Help furnish the proper information on which the reports of surveyors and others are to be based;
- Insist that the reports be rendered promptly; and
- Examine the reports critically to the extent possible, because errors can always occur.

Surveyors or engineers should be retained to ascertain whether metes and bounds are correct and whether the property is subject to unrecorded defects such as encroachments, shifting water boundaries, subsidence, or structural defects. (Licensed engineers are authorized to perform surveys as long as they pass the examination required by Bus & P C §§8731 and 8741(b). They are referred to in this chapter as surveyors.)

An attorney whose responsibilities have been carried out properly will not be responsible for errors in the surveyor's report. When appropriate, however, the lawyer should:

- Counsel clients on the need for a surveyor;
- State the problem correctly to the surveyor;
- Check the complete report; and
- Question the surveyor about any aspects of the report that appear incorrect.

In drafting subdivision and survey maps, the law requires employment of a licensed surveyor. See §11.12. In using the California Coordinate System (explained in §§11.22-11.23), the difficulty of understanding and interpreting courses makes a surveyor indispensable. In describing the effects of off-record matters affecting descriptions (see §§11.53-11.57, 11.77-11.79), prudence often dictates hiring a professional surveyor.

© The Regents of the University of California

II. FINDING CORRECT DESCRIPTIONS

§11.9 A. Deeds

Ordinarily, the seller should be able to produce the deed, judgment, or other document by which he or she acquired title to the property. If not, either a title company or the recorder's office can readily produce a copy. This document cannot always, however, be relied on to describe the property accurately: The seller may be parting with only a fraction of the property described in his or her documents of title, or the description may have been changed by subsequent matters of record, such as condemnation or partial conveyances, or by events that do not show on the record, such as easements, adverse possession, prescription, or implied dedication. See §§11.53-11.57, 11.77-11.79; see also California Easements and Boundaries: Law and Litigation (Cal CEB 2008).

It should also not be assumed that the previous description does not contain survey errors or does not misdescribe all or a portion of the property.

© The Regents of the University of California

§11.10 B. Preliminary Report or Title Insurance Policy

The seller's lawyer should ask to see the client's title insurance policy (Ins C §12340.2) before the seller enters into a sale transaction and should view it in the proper context. Title insurance is a contract of indemnity against loss through defects in the title or liens or encumbrances that affect the title; unlike an abstract of title or a survey, it is not a representation of the property description or status of title. *Lawrence v Chicago Title Ins. Co*. (1987) 192 CA3d 70, 74, 237 CR 264. See California Title Insurance Practice §§5.25-5.29 (2d ed Cal CEB 1997). There is no coverage for physical conditions of property that merely affect land value (*Hocking v Title Ins. & Trust Co.* (1951) 37 C2d 644, 651, 234 P2d 625) or restrictions created by generally applicable ordinances (*Elysian Inv. Group v Stewart Title Guar. Co.* (2002) 105 CA4th 315, 323, 129 CR2d 372). The policy reflects the status of the title of the property and is effective as of the date it was issued, and it will not reflect subsequent events, which may have altered or affected the description. *Quelimane Co. v Stewart Title Guar. Co.* (1998) 19 C4th 26, 41, 77 CR2d 709. Some of these matters are discussed in §§11.77-11.79. To discover possible changes in the description, both parties should obtain the additional information enumerated from inspections, surveys, and title services (see §§11.11-11.13).

As part of this information, it is customary and prudent to order a preliminary report. Ins C §12340.11. On preliminary reports generally, see Title Ins, chap 5. The report may include a copy of a parcel map, but more often a copy of an assessor's parcel map is attached for information only and usually bears a stamp or legend to that effect. Assessor's maps can be convenient, but they should be used with great care. They are not legal descriptions and do not impart constructive notice under the recording laws (CC §§1213-1215). They are nothing more than compilations from various sources deemed accurate by the staff at the assessor's office, and their quality varies widely. Inaccuracies in descriptions are not always detectable, and the information is not necessarily complete. In addition, lot lines may have been eliminated for convenience or, because of common ownership, to simplify tax collection records. If recorded parcel maps or surveys are available, it is prudent to request a copy of one.

PRACTICE TIP: Because the preliminary report does not insure the description, buyers should protect themselves by acquiring a binder or conditioning the purchase and sale agreement on review and approval of the description and any acceptable exceptions to title, and receipt of a title insurance policy insuring title as approved by the buyer. For a discussion of title insurance, see §§4.50-4.55. See also Title Ins §§5.25-5.28, 11.38-11.44.

In reviewing title insurance policies for information on descriptions and the status of title, the type of policy and any endorsements to it must be considered. Commonly issued California Land Title Association (CLTA) forms are generally underwritten, based on matters of record at the recorder's office only. American Land Title Association (ALTA) forms insure against a number of off-record risks; a survey can be prepared and incorporated by a CLTA 116.1 endorsement that insures that the property described in the title policy is the same as is shown on the survey attached to the policy, subject to any noted exceptions. The usefulness of a given title insurance policy in reviewing descriptions will depend on the type of policy, its issuance date, and the client's objectives. On structure and coverage of title insurance policies, see Title Ins, chap 6. On owner's policies and endorsements, see Title Ins, chap 7.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/11 Descriptions of Property/§11.11 C. Inspection of Premises

§11.11 C. Inspection of Premises

A bona fide purchaser is charged with notice of matters inconsistent with record title discoverable by inspection of the property. CC §19; *Caito v United Cal. Bank* (1978) 20 C3d 694, 702, 144 CR 751; *Scheerer v Cuddy* (1890) 85 C 270, 273, 24 P 713; *Melendez v D & I Inv., Inc.* (2005) 127 CA4th 1238, 1251, 26 CR3d 413; *Gates Rubber Co. v Ulman* (1989) 214 CA3d 356, 262 CR 630.

Possession of land is notice of whatever right, title, or interest the occupant may have in the property, and puts all persons on inquiry to determine how and under what right the occupant holds possession. See *Pacific Gas & Elec. Co. v Minnette* (1953) 115 CA2d 698, 252 P 2d 642. Nevertheless, according to the "form of title" presumption, the description in a deed as to how title is held is presumed to reflect the actual ownership interests in the property, as codified in Evid C §662, and this presumption may be rebutted only by clear and convincing proof. *Marriage of Brooks* (2008) 169 CA4th 176, 185, 86 CR3d 624.

A description from a deed or title insurance policy should in most circumstances be checked by inspecting the land, which can occur through one or more inspections by the following:

- The client or its staff;
- Real estate brokers;
- Attorneys;
- Licensed surveyors; and
- Title officers.

The buyer may be charged with notice of information that he or she could have obtained by questioning a party whose possession of the property is inconsistent with record title. In *In re Weisman* (9th Cir 1993) 5 F3d 417, 420, a bankruptcy trustee trying to qualify as a bona fide purchaser would have learned from the ex-husband in possession that the former wife had conveyed the property to him by unrecorded quitclaim. See also *In re Whiting* (2004) 311 BR 539, 543. A purchaser is charged with knowledge of the following:

- The nature of the property;
- Its current use;
- The identities of the persons occupying it;
- The relationships among them; and
- The relationship between those in possession and the purported seller.

Real estate brokers, although charged with limited duties of inspection and disclosure of facts materially affecting the value or desirability of the property (*Easton v Strassburger* (1984) 152 CA3d 90, 199 CR 383), cannot realistically be expected to possess the expertise to notice much more than obvious discrepancies in record title. The attorney's inspection can be a great advantage to the client, but his or her expertise may not exceed the ability to confirm that a surveyor should be employed. Licensed surveyors, because of their unique technical expertise, are the most qualified persons to check descriptions and monuments. Use of a surveyor will depend on the type of transaction and the client's objectives. Title officers seldom perform inspections unless an American Land Title Association (ALTA) owner's policy with survey endorsement is requested. In any large transaction, a field inspection will almost certainly occur, although the title insurer may also rely on the surveyor's reputation in issuing its ALTA survey endorsement. On inspections and survey requirements for extended coverage insurance policies, see California Title Insurance Practice §§2.13, 4.31 (2d ed Cal CEB 1997).

An inspection may also disclose survey monumentation, along with other monuments such as street rights-of-way or markers. Aerial photographs can also be useful for large tracts, particularly in evidencing easements or encroaching fences.

Third party rights should be ascertainable on an inspection, as evidenced by fences, driveways, easements, power lines, pipeline signs, or persons in possession of part or all of the property.

© The Regents of the University of California

§11.12 D. Surveys and Engineering Studies

Some problems are discoverable only by engineers and surveyors. If the seller has conducted a recent survey, he or she may make it available to the buyer. If not, the attorney's failure to advise the hiring of an engineer or a surveyor in a proper case may be a disservice to the client. Ideally, qualified surveyors should draft all new descriptions. They are required by law to do so in drafting subdivision and survey maps. Govt C §§66495-66496. Their services should also be used when there is any question of encroachment, uncertain boundaries, possible landslides, or similar defects.

Sometimes, however, surveyors assume without question that a fence or a line between adjacent buildings correctly marks a boundary. When the assumption is open to question, the lawyer may have to insist that the line be accurately measured.

Issuance of some title insurance policies may be based on approval by the title insurer of an American Land Title Association (ALTA) survey or similar service by a surveyor. Use of surveyors should be coordinated with the requirements of the title insurers involved in the transaction. On ALTA surveys, see California Title Insurance Practice §4.32 (2d ed Cal CEB 1997).

For articles discussing surveys, see York, *Surveys in Real Property Transactions—Parts I-II*, 5 CEB Real Prop L Rep 121, 145 (Oct., Nov. 1982), and additional comments in Cummins, *Comment on Surveys in Real Property Transactions*, 6 CEB Real Prop L Rep 57 (Apr. 1983).

© The Regents of the University of California

§11.13 E. Title Services

The client's ultimate protection regarding the legal description is often a title insurance policy in proper form and with proper policy limits. It is important that the policy limits reflect not only the purchase price but any potential improvements and expenditures that a client may make to the property. In addition to advising the client on the proper form of policy, the attorney should also discuss the availability of standard or specialized endorsements. On advising clients on title insurance, see California Title Insurance Practice, chap 2 (2d ed Cal CEB 1997).

Title officers can also be used for informal assistance. In such discussions, it is important to bear in mind that title insurance is a contract of indemnity and that the title company will view the provision of information as preliminary to the issuance of its policy, and that it is assuming no greater obligation than that ultimately reflected in the policy itself. Unless a specific abstract of title is requested under Ins C §12340.10, a title insurer may not be liable for any negligent errors or misrepresentations made in giving informal advice. On liability under preliminary reports, see Title Ins §§5.25-5.28, 11.38-11.44. In this context, title officers can often help clients or lawyers with the following tasks:

- Read complicated descriptions and indicate or identify property as described on a plat (which, however, may yield to survey marks "on the ground" if the two conflict);
- Approve legal descriptions acceptable for title insurance purposes from record information, an approved survey, or both, the source of information depending on the title service rendered;
- Verify that the bearings and distances shown in a metes and bounds description (see §§11.26, 11.90) are mathematically correct and that the complete description is sufficient to enclose and identify the particular parcel; and
- In conjunction with extended coverage title insurance, verify and correlate survey and record information to learn whether discrepancies exist that will require remedial action. On surveys, see Title Ins §§4.30-4.34.

California title companies do not, however, offer surveying services as such.

© The Regents of the University of California

III. READING DESCRIPTIONS

§11.14 A. Certainty Requirement

The cardinal rule in construing descriptions is to discover and carry out the parties' intentions. *City of Manhattan Beach v Superior Court* (1996) 13 C4th 232, 238, 52 CR2d 82. A description of real property is generally sufficient if it identifies the land or furnishes the means of designating the property sought to be conveyed. It has been held that, if a competent surveyor can take the description and locate the land with or without the aid of extrinsic evidence, the description is sufficient. *Daluiso v Boone* (1969) 269 CA2d 253, 262, 75 CR 287. If the description is not sufficiently certain, the conveyance can be voided. *Morehart v County of Santa Barbara* (1994) 7 C4th 725, 766, 29 CR2d 804; *Saterstrom v Glick Bros. Sash Co*. (1931) 118 CA 379, 5 P2d 21.

In the purchase and sale agreement, the description must be certain enough to satisfy the statute of frauds (CC §1624(a)(3); CCP §1971) and be specifically enforceable (CC §3390). Although less certainty is required in a contract to convey land than in the conveyance document itself, the description must be sufficient, without parol evidence, to locate the property. *Calvi v Bittner* (1961) 198 CA2d 312, 17 CR 850. But see §11.15.

© The Regents of the University of California

§11.15 B. Ambiguity

Mere ambiguity is not fatal if it can be cured by parol or extrinsic evidence. *Fudickar v East Riverside Irrig. Dist*. (1895) 109 C 29, 41 P 1024. Extrinsic evidence is inadmissible to add to, detract from, or vary the terms of the deed, but it is admissible to ascertain the issue involved when an ambiguity appears on the face of the deed. *Severns v Union Pac. R.R. Co.* (2002) 101 CA4th 1209, 1214, 125 CR2d 100; *Concord & Bay Point Land Co. v City of Concord* (1991) 229 CA3d 289, 294, 280 CR 623; *Baker v Ramirez* (1987) 190 CA3d 1123, 1132, 235 CR 857. The intent must be discovered according to statutory and judicial rules of construction. See CCP §§1857, 1866, 2077; CC §§830-831, 1069, 1112; Govt C §§23071-23076; *White v State* (1971) 21 CA3d 738, 766, 99 CR 58. The directive of CC §1069 that a grant by a public agency is to be interpreted in favor of the grantor applies only if the grant is ambiguous. *Red Mountain LLC v Fallbrook Pub. Util. Dist.* (2006) 143 CA4th 333, 344, 48 CR3d 875.

Although parol evidence is admissible to allow the description to be identified with its location on the ground (*Calvi v Bittner* (1961) 198 CA2d 312, 17 CR 850), it is not admissible to supply a description when the writing does not furnish the means to make it certain (*Alameda Belt Line v City of Alameda* (2003) 113 CA4th 15, 21, 5 CR3d 879; *Vezaldenos v Keller* (1967) 254 CA2d 816, 823, 62 CR 808). See *Finn v Goldstein* (1927) 201 C 605, 258 P 85 (description by address sufficient when it includes entire property); *Kapner v Meadowlark Ranch Ass'n* (2004) 116 CA4th 1182, 1187, 11 CR3d 138 (reference to previously recorded CC&Rs that contained metes and bounds description of property); *Brudvig v Renner* (1959) 172 CA2d 522, 342 P2d 276 (description by address insufficient when undescribed portion excluded); *Roberts v Lebrain* (1952) 113 CA2d 712, 248 P2d 810 (description by street alone insufficient when seller owned two residential properties on same street).

If the parties' intentions are ascertainable from the instrument itself, parol evidence is inadmissible. *Joerger v PG&E* (1929) 207 C 8, 276 P 1017; *Severns v Union Pac. R.R. Co.* (2002) 101 CA4th 1209, 1214, 125 CR2d 100. However, without evidence that the parties intended a completely integrated writing, parol evidence is admissible to prove a meaning to which a deed is reasonably susceptible. *Masterson v Sine* (1968) 68 C2d 222, 65 CR 545. As in any contract, the primary object of interpretation of a deed is to ascertain and carry out the intention of the parties. Applicable rules of interpretation must be considered, given their proper weight, and construed in light of extrinsic evidence that may prove a meaning to which the instrument's language is reasonably susceptible. *City of Manhattan Beach v Superior Court* (1996) 13 C4th 232, 52 CR2d 82; *City & County of San Francisco v Union Pac. R.R. Co.* (1996) 50 CA4th 987, 58 CR2d 1. In *PG&E v G.W. Thomas Drayage & Rigging Co*. (1968) 69 C2d 33, 69 CR 561, the court held that extrinsic evidence is admissible to prove a meaning to which the language of a written agreement is reasonably susceptible, even though on its "four corners" the instrument appears to the court to be clear and unambiguous.

An agreement may be sufficiently certain to permit damages for breach but insufficiently certain for specific performance. See *Brudvig v Renner, supra*. On damages for seller's breach, see California Real Property Remedies and Damages, chap 4 (2d ed Cal CEB 2002).

© The Regents of the University of California

§11.16 C. Acreage Problems

A statement of acreage as part of a description is not common and could either create an ambiguity or resolve one. For example, since a government survey section may not be exactly one mile square (see §11.17), the addition of the language "consisting of 640 acres" may create an ambiguity. Thus the words "more or less" are generally added if acreage is given. On a plat, "more or less" may be expressed by the symbol ± (as in Figure 1, §11.18). An erroneous statement of acreage adds nothing to a description if it is otherwise clear that the grantor intended or was obligated to transfer title to an entire parcel. As discussed in §11.11, buyers are charged with constructive notice of all facts that an inquiry could reveal. CC §19. Typically, this inquiry includes the area of the property and, in the absence of fraud by the seller, the buyer is generally charged with notice of the acreage involved. It is the author's view that including the acreage may be appropriate in purchase and sale agreements in reference to price and other aspects of the transaction, but it is not appropriate in the legal description itself. Also, references to acreage can be relative. Parties may or may not deduct easements or rights-of-way, and it may be unclear whether calculations are made to the edge of adjacent rights-of-way, the physical placement of a road surface (which may or may not be on the edge of the right-of-way of record), or to the centerline presumed under CC §1112.

PRACTICE TIP: In transactional documents, it is best to refer specifically in the description to each potential ambiguity revealed by the record or an inspection. If the entire fee is to be conveyed, but the price is to be computed on less than the gross area, two different descriptions will be used in the same transaction.

© The Regents of the University of California

§11.17 D. Reference to Government Surveys

The rectangular system of surveying was adopted by the federal government in 1785. This system generally provides for townships six miles square, containing 36 sections, each approximately one mile square.

Lawyers commonly encounter descriptions based on United States government surveys, particularly in large parcels of rural land or in reviewing chains of title of subdivided properties. These surveys have been applied generally to public lands in all states north of the Ohio River and all states west of the Mississippi River except Texas. They have also been used in Alabama, Mississippi, and Florida. The surveys divide the land into rectangular units as outlined in Bureau of Land Management, Manual of Instructions for the Survey of the Public Lands of the United States (1973). For information on the next edition of this manual, see Directory. For assistance in reading these descriptions, see Wattles, Writing Legal Descriptions in Conjunction With Survey Boundary Control (4th ed 1981).

A typical description based on these rectangular surveys is, *e.g.,* "southwest ¼ of southwest ¼ of southwest ¼, section 36, township 2 north, range 4 east, Mount Diablo base and meridian." The land described by this formula is the smallest shaded plot in Figure 1, §11.18. Sometimes the description is abbreviated. Thus, the above description may appear as "SW ¼ of SW ¼ of SW ¼ S 36 T2N R4E MDB&M" or as "SW ¼ of SW ¼ of SW ¼, Sec 36, Twp 2N, Range 4E, Mount Diablo B&M."

NOTE: Generally, although abbreviations are desirable on maps, authorities recommend that descriptions be spelled out in conveyances and agreements in order to avoid inadvertent errors. See Brown, Robillard, & Wilson, Evidence and Procedures for Boundary Location (3d ed 1994). Potential ambiguity results from the omission of "of" or "and" in a description containing a series of quarter sections. For example, does "SE ¼ SW ¼" mean both the southeast quarter and the southwest quarter or only the southeast quarter of the southwest quarter?

In reading a description based on a government rectangular survey, the best way to locate the land on a map is to read the description backwards; this method is explained in §11.21.

The survey of public lands creates the boundary lines, and a description of land granted by U.S. patent is final; however, extrinsic evidence can be admissible to explain uncertainties of the grant and to determine original intent. *Claudino v Pereira* (2008) 165 CA4th 1282, 1288, 82 CR3d 464.

© The Regents of the University of California

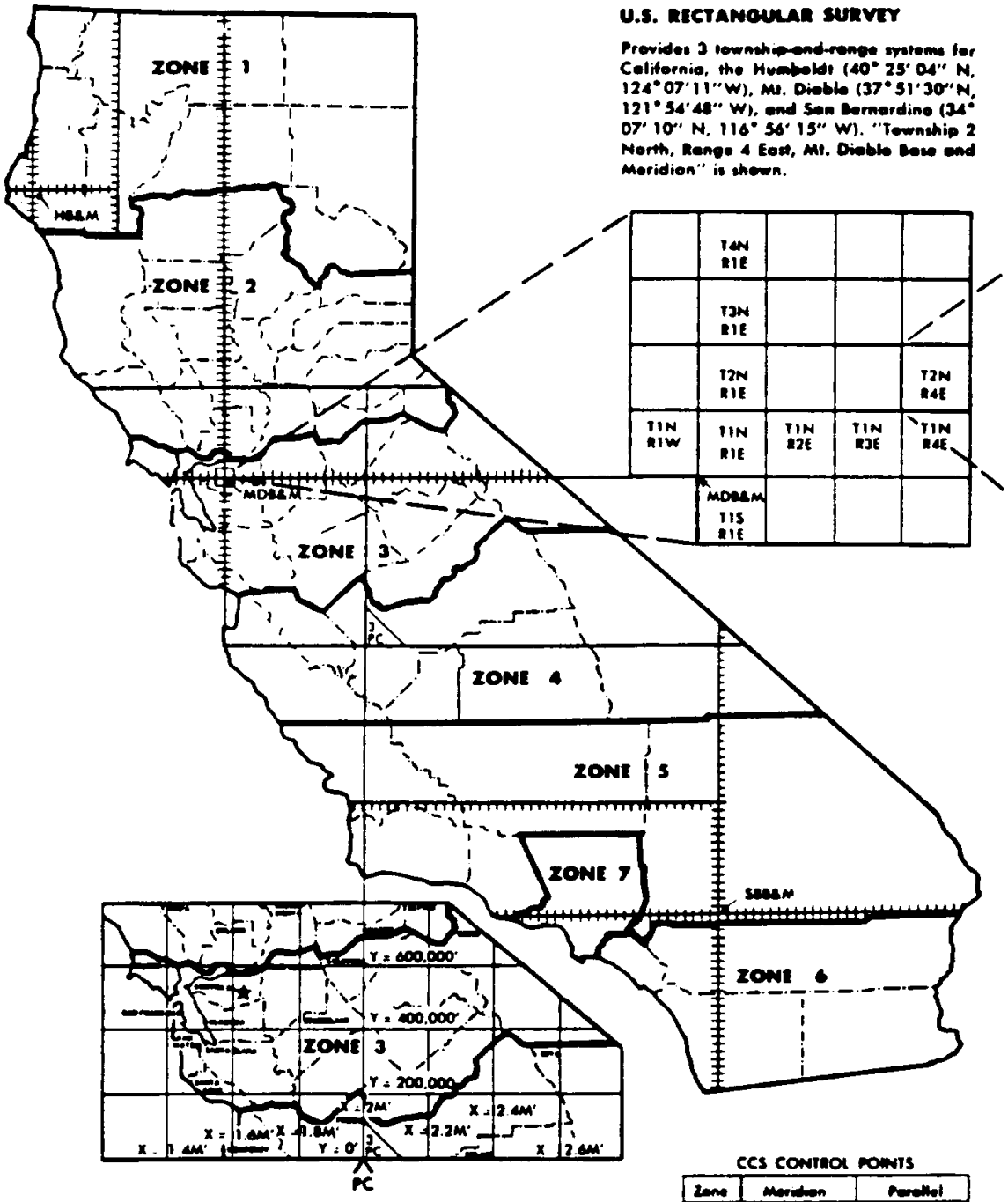
Source: Real Property/California Real Property Sales Transactions/11 Descriptions of Property/§11.18 1. Base and Meridian

§11.18 1. Base and Meridian

After California became a state in 1850, federal surveyors divided the state into townships. Three base and meridian landmarks were designated. In Northern California, the surveys were based on the Humboldt base and meridian, in Central California on the Mt. Diablo base and meridian, and in Southern California on the San Bernardino base and meridian. The surveyors then projected north-south lines through the base points and named them principal meridians, and projected east-west lines through the base points and named them base lines. The initials "MDB&M" in the description refer to the Mt. Diablo base and meridian system, defined by the intersection of the Mt. Diablo base and the Mt. Diablo meridian. All three base and meridian systems are shown on the map of California in Figure 1 below.

Print

California Coordinate and U.S. Rectangular Systems



U.S. RECTANGULAR SURVEY

Provides 3 township-and-range systems for California, the Humboldt (40° 25' 04" N, 124° 07' 11" W), Mt. Diablo (37° 51' 30" N, 121° 54' 48" W), and San Bernardino (34° 07' 10" N, 116° 56' 15" W). "Township 2 North, Range 4 East, Mt. Diablo Base and Meridian" is shown.

CALIFORNIA COORDINATE SYSTEM

Divides state into 7 zones and prescribes a point of control (PC) for each (Pub Res C §§8801–8816). A point of control is the intersection of a meridian (for Zone 3, 120° 30' W) given the value X (East) = 2,000,000 feet, and a parallel (for Zone 3, 36° 30' N) at which Y (North) = 0 feet. Adjustment factor commonly shown converts sea level distances of system to ground level. Coordinates of this point ★ are X = 1,675,000, Y = 525,000, CCS, Zone 3, Factor 1.0000546.

CCS CONTROL POINTS

Zone	Meridian	Parallel
1	122° W	39° 20' N
2	122° W	37° 40' N
3	120° 30' W	36° 30' N
4	119° W	35° 20' N
5	118° W	33° 30' N
6	116° 15' W	32° 10' N
7	118° 20' W	34° 08' N

Print

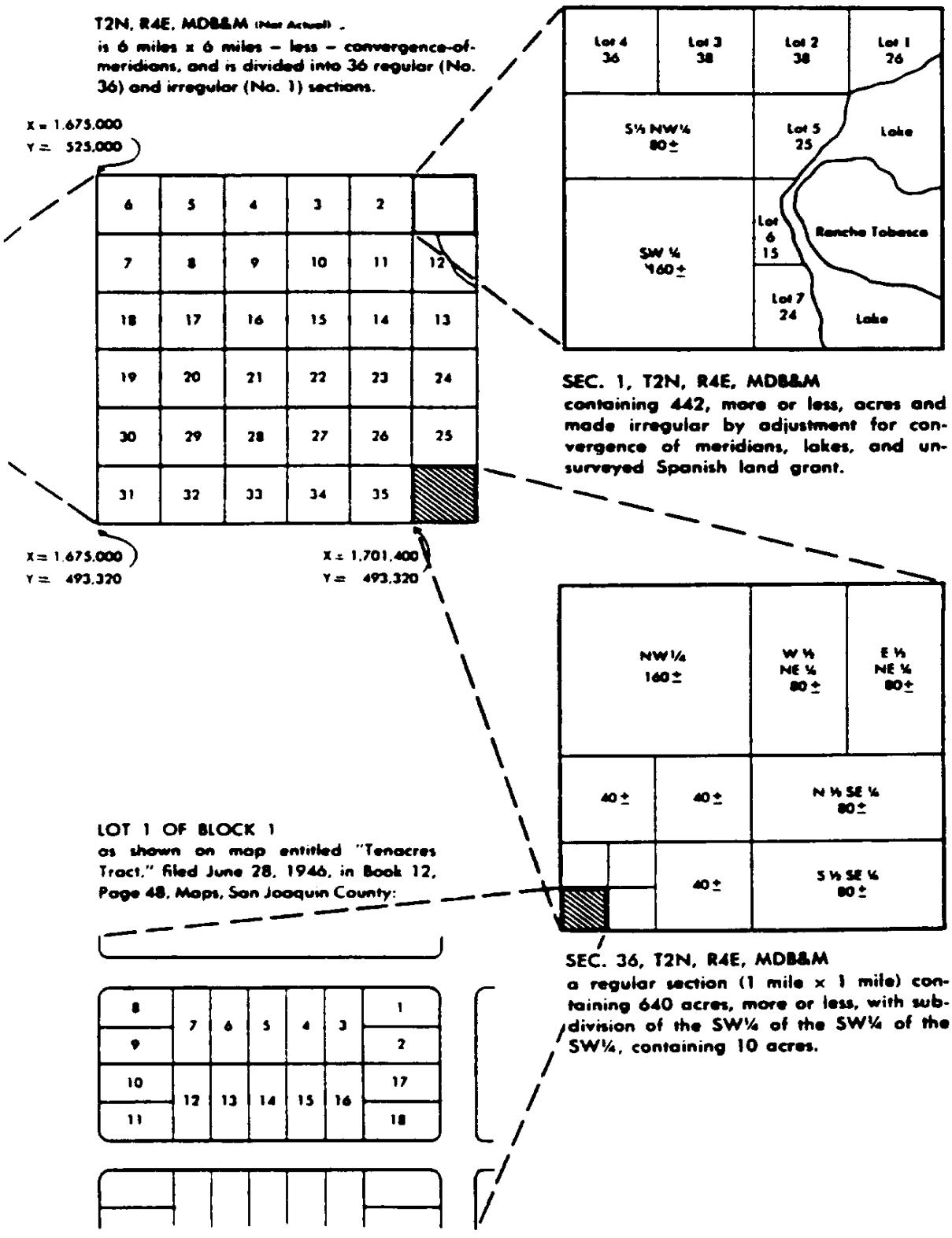


FIGURE 1

© The Regents of the University of California

§11.19 2. Range and Township

In the description "southwest ¼ of southwest ¼ of southwest ¼, section 36, township 2 north, range 4 east, Mt. Diablo base and meridian," the element "range 4 east" refers to the fourth range east of the Mt. Diablo meridian. Each range is approximately six miles wide (subject to variations due to the convergence of meridians as they go northward); the ranges are numbered consecutively, east or west from the applicable meridian. For example, the first range to the west of the meridian would be "range 1 west."

Township lines occur at six-mile intervals north and south of bases. Thus, the designation "township 2 north" in the description above refers to a township in the second tier north of the Mt. Diablo base in the specified range (range 4 east) and describes an area of approximately 36 square miles. As a matter of convention, the township always precedes the range in descriptions.

© The Regents of the University of California

§11.20 3. Section

The element preceding the designation of township and range is usually a section number. In the example given in §11.19, the section described is section 36. A township ordinarily consists of 36 sections, each approximately one mile square, *i.e.,* approximately 640 acres. In the same way that meridians and range boundaries converge as they approach the North Pole, the north-south boundaries of sections also converge. As a result, sections rarely measure a perfect square mile. For this reason, the words "more or less" should be used if the area or acreage of a section is given at all. On the question of whether to add acreage to the description, see §11.16.

© The Regents of the University of California

§11.21 4. Quarters

Sections are commonly subdivided into quarters or halves, and this quartering or halving may be carried down into further quarters or halves. In the description "southwest ¼ of southwest ¼ of southwest ¼, section 36," the quarter reference preceding the section number refers to the southwest quarter of section 36. In Figure 1, §11.18, that is the quarter consisting of four approximately 40-acre squares (three notated "40±", one shaded); a total of 160 acres, more or less. The middle "southwest ¼" refers to the southwest quarter of the 160-acre quarter. And the first "southwest ¼" describes the shaded 10-acre parcel in the diagram of section 36 in Figure 1. As shown in the illustration, that parcel may be further subdivided (*e.g.,* into lots, quarters, halves, or parcels described by metes and bounds; see §11.18).

© The Regents of the University of California

E. California Surveying Systems

§11.22 1. California Coordinate System of 1927

An optional system of describing land is the California Coordinate System of 1927 (CCS). See Pub Res C §§8801-8819. The CCS is based on the "system of plane coordinates which has been established by the United States Coast and Geodetic Survey for defining and stating the positions or locations of points on the surface of the earth within the State of California." Pub Res C §8801(a). The system is based on the fact that the earth is an oblate spheroid rather than a perfect sphere; seven spheroids of reference or zones are created. Pub Res C §§8803-8809. The rectangular system discussed in §11.17 is not based on the Coast and Geodetic Survey, but on Bureau of Land Management surveys.

In drafting a description, CCS coordinates are superfluous in most instances: To constitute constructive notice—which is at the very heart of the recording laws (see §§15.85-15.92)—the description must contain sufficient data to identify the property without recourse to the coordinates; in a conflict between the two descriptions, the coordinates yield to the other description. Pub Res C §8814; see MacEllven, Coordinate Surveying System, California Land Title Association Proceedings 32 (1958).

In reading a CCS description, lawyers concerned with accuracy and potential liability will not rely on their own skill alone. The location of a point consists of a measurement in feet, east or west from a north-south axis parallel to a stated meridian and north or south from an axis at right angles to that meridian. An example of this kind of description is shown below the map of California in Figure 1, §11.18. The system is primarily an aid to surveyors but is of limited effect in describing land for conveyances.

© The Regents of the University of California

§11.23 2. Alternative Surveying and Mapping Systems

In addition to the California Coordinate System of 1927, newer systems of surveying and mapping have been adopted in California: the California Coordinate System of 1983, based on the National Geodetic Survey known as the North American Datum of 1983 (Pub Res C §8801(b)); and a California Spatial Reference System-Horizontal, based on Global Positioning System survey methods using satellites (Pub Res C §8801(e)).

© The Regents of the University of California

§11.24 F. Subdivision or Parcel Maps

In the modern context, subdivision or parcel maps are the most common and most desirable method of describing parcels, but the method is not immune from survey errors or other mistakes.

Property may be described by reference to a recorded map. *McCullough v Olds* (1895) 108 C 529, 41 P 420. The advantage of this method is that the property's relationship to surrounding properties and appurtenances such as easements is readily demonstrated. The filing of a map is deemed a declaration of the right to use streets and passageways abutting a lot as well as the streets and ways leading to public places on highways, all of which pass in subsequent conveyances that refer to the description on the map. *Danielson v Sykes* (1910) 157 C 686, 109 P 87. The two requirements for the validity of this type of description are the following:

- The document can be produced and identified and the land located from the descriptive data (see §§11.14-11.16); and
- The map must be properly recorded, usually in a special map book maintained by the County Recorder.

The requirements for recordation of maps are set out in Govt C §§66410-66499.37 (Subdivision Map Act; see also 10 Cal Code Regs §§2790-2804); Govt C §§66499.50-66499.58 (official maps of cities, towns, and counties); Bus & P C §§8762-8771.5 (record of survey maps; see also 16 Cal Code Regs §465); Rev & T C §327 (assessors' maps); Health & S C §§8550-8557 (cemeteries); and CC §§1350-1359 (condominiums). Contracts for the sale, lease, or financing of real property for which a final map is pending must be expressly conditioned on the approval and filing of a final subdivision map. Govt C §66499.30(e). See *Sixells, LLC v Cannery Bus. Park* (2008) 170 CA4th 648, 652, 88 CR3d 235 (purchase conditioned on waiver of recordation of final subdivision map violates statute); *Black Hills Invs., Inc. v Albertson's, Inc.* (2007) 146 CA4th 883, 892, 53 CR3d 263. A transfer in violation of the Subdivision Map Act is voidable at the option of the grantee or the grantee's successor in interest within 1 year after discovery of the irregularity. Govt C §66499.32. See generally California Subdivision Map Act and the Development Process §§8.1-8.2 (2d ed Cal CEB 2001). Descriptions should not be drafted with reference to assessors' maps, because the distances and courses on these maps are not always accurate. See §11.10. For forms showing how to draft descriptions referring to recorded maps and other proper documents, see §§11.99-11.103.

For validity of ancient (pre-1893) maps, refer to the discussion in *Gardner v County of Sonoma* (2003) 29 C4th 990, 129 CR2d 869, and *Morehart v County of Santa Barbara* (1994) 7 C4th 725, 29 CR2d 804.

© The Regents of the University of California

§11.25 G. Reference to Other Recorded Instruments

As long as the necessary elements for constructive notice are present, usually through recordation under the recording laws (CC §§1169-1172, 1213-1218), property can also be described by reference to earlier deeds or instruments. *Central Pac. R.R. v Beal* (1873) 47 C 151. This is a somewhat cumbersome method because the earlier instrument must be both located and plotted. This method was in common use before the rise of parcel maps, but it is particularly susceptible to ambiguity or error when monuments have disappeared or are inconsistent. A reference to unclear language in an old deed in specifying a boundary or a point of beginning may be a good indication of the need for a survey.

A reference to public rights-of-way (*i.e.,* "bounded by that certain public highway") is also common and may also lead to ambiguities. A public right-of-way of record may differ from the physical existence of the street or paving; it is not unusual for municipalities to construct a street within but not necessarily up to the edge of the right-of-way grant, and detecting the difference may require a surveyor's expertise. Likewise, public rights-of-way are often easements instead of fee title (see *People v Thompson* (1954) 43 C2d 13, 19, 271 P2d 507; *City of Los Angeles v Pacific Elec. Ry. Co.* (1959) 168 CA2d 224, 228, 335 P2d 1042; CC §§831, 1112), and it may not be clear whether a reference to a street meant the edge or the centerline, even though certain presumptions may apply. On rights of way, see California Easements and Boundaries: Law and Litigation, chap 7 (Cal CEB 2008).

© The Regents of the University of California

§11.26 H. Metes and Bounds Descriptions

Metes and bounds descriptions are perhaps the most common type of description and are often confusing to those who are unfamiliar with the basic principles of this kind of description. The system is generally based on an established point of beginning, with a series of courses containing compass bearings and distances, until a tract of land is described and the courses return or "close" at the point of beginning. Courses containing curves are based on radius definitions, which are particularly confusing to laymen. The bearings themselves are based on lines of direction from the points of the compass, north or south, or east or west.

A description by metes and bounds may combine two or more of the kinds of references described in §§11.27-11.39, and it may be combined with descriptions other than metes and bounds, as in the second example in §11.38.

© The Regents of the University of California

§11.27 1. Natural Monuments

Natural monuments include rivers, trees, and rocks. *Mammoth Gold Dredging Co. v Forbes* (1940) 39 CA2d 739, 751, 104 P2d 131. Generally, a reference to natural monuments is less desirable than surveyors' calls: the course of a river may change, the point of a hill may be eroded, a tree may die, or a rock may give way to natural forces or construction. *Maginnis v Hurlbutt* (1917) 34 CA 504, 510, 168 P 368.

© The Regents of the University of California

§11.28 2. Artificial Monuments

Artificial monuments placed by surveyors, particularly as a reference point for beginning a metes and bounds description, are common. The monument may consist of little more than a metal plate bearing the surveyor's license number and job number, and it may be set it in the ground with a sledgehammer or cast in concrete. Although widely used, these monuments are also subject to loss through erosion, soil subsidence, vandalism, later improvements, and even earthquakes.

Artificial monuments also include references to existing walks, fences, buildings, railroads, stakes, streets, and so forth. Because such structures may be removed or destroyed, they are considered less desirable as reference points.

© The Regents of the University of California

§11.29 3. Adjoining Lands

Another method of describing property is by reference to adjoining lands.

EXAMPLE: This is a description of property by adjoining lands:

> [B]ounded on the north and west by the lands of A.R. Smith per deed recorded at book 9, page 2, Misc. Records, and on the south and east by the Gonzalez Ranch per decree of distribution recorded at book 14, page 112 of Judgments, office of County Recorder, County of Nevada, State of California.

Well-drafted descriptions of this type consist of more than just the names of the properties or their owners. In this example, the description refers to recorded instruments. The requirements of descriptions by reference to recorded instruments are discussed in §11.25. For an example of a description by reference to names only, see *McKeon v Millard* (1874) 47 C 581.

© The Regents of the University of California

§11.30 4. Streets and Public Rights-of-Way

Streets and public rights-of-way are also commonly used as points of beginning. Care must be taken to state whether the parties intend to refer to the edge of the right-of-way of record or to the pavement as physically placed, as the case may be. A grant will normally be construed to the center of a highway unless a different intent appears from the grant. CC §1112; *Neff v Ernst* (1957) 48 C2d 628, 635, 311 P2d 849.

For a discussion of historical roads, see *Western Aggregates, Inc. v County of Yuba* (2002) 101 CA4th 278, 130 CR2d 436. For a discussion of common law dedication, see *Hanshaw v Long Valley Road Ass'n* (2004) 116 CA4th 471, 11 CR3d 357. On the applicability of the public trust doctrine to the closure of streets in reclaimed tidelands, see *Zack's, Inc. v City of Sausalito* (2008) 165 CA4th 1163, 1194, 81 CR3d 797.

© The Regents of the University of California

§11.31 5. Railroad Rights-of-Way

Several cases have made it clear that land can be described by reference to railroad right-of-way easements as borders. These descriptions imply ownership to the center of the easement. See *Millyard v Faus* (1968) 268 CA2d 76, 73 CR 697; *Freeman v Affiliated Prop. Craftsmen* (1968) 266 CA2d 723, 72 CR 357; *Faus v Nelson* (1966) 241 CA2d 320, 50 CR 483. These cases applied the long-established monument doctrine, which presumes an intent to grant to the middle of the monument when it is used to describe a property boundary. *Freeman v Bellegarde* (1895) 108 C 179, 41 P 289. The same rule applies when land is sold with reference to a recorded map that shows a street or railroad right-of-way easement as bounding the property. *Freeman v Affiliated Prop. Craftsmen, supra*.

NOTE: Issues may arise about whether the railroad right-of-way was originally acquired as an easement or in fee. See *City of Manhattan Beach v Superior Court* (1996) 13 C4th 232, 52 CR2d 82 (original grantor's intent could not be determined from original deed, which contained conflicting quitclaim and right-of-way provisions, but extrinsic evidence of conduct subsequent to original conveyance indicated that title had been transferred); *Severns v Union Pac. R.R. Co.* (2002) 101 CA4th 1209, 125 CR2d 100 (fee simple, stipulated to by both parties; but because plaintiff did not timely record intent to preserve future interest following abandonment, power to terminate expired).

In *Millyard v Faus, supra,* the rule of *Faus v Nelson, supra,* was carefully limited to easements for railroad rights-of-way and was not extended to include an easement for a railroad depot. On railroad easements, see California Easements and Boundaries: Law and Litigation, chap 7 (Cal CEB 2008).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/11 Descriptions of Property/ 6. Courses and Distances/§11.32 a. Bearings and Degrees

6. Courses and Distances

§11.32 a. Bearings and Degrees

The directions or courses of metes and bounds descriptions are computed on a quadrant system of direction. Angular measurements are made with respect to a line due north and south (the cardinal line of the true meridian) either easterly or westerly to a maximum of 89°, 59', 59". A course of 90° would be either due east or due west.

Bearings due north, south, east, or west require no numbers (but see §11.39 on identifying north bearings). Bearings that deviate from those four directions require numbers to indicate the angle of deviation. Between, *e.g.,* north and west, the difference in angle is ninety degrees (90°). One-ninetieth of that angle is one degree. Each degree is divided into sixty minutes (60') and each minute into sixty seconds (60"). Thus, the angle between north and west is divisible into 324,000 angles of one second each. (At a distance of ten miles from the point of angle, a deviation of one second results in a difference of about three inches; a deviation of one minute makes a difference of about 14 feet.)

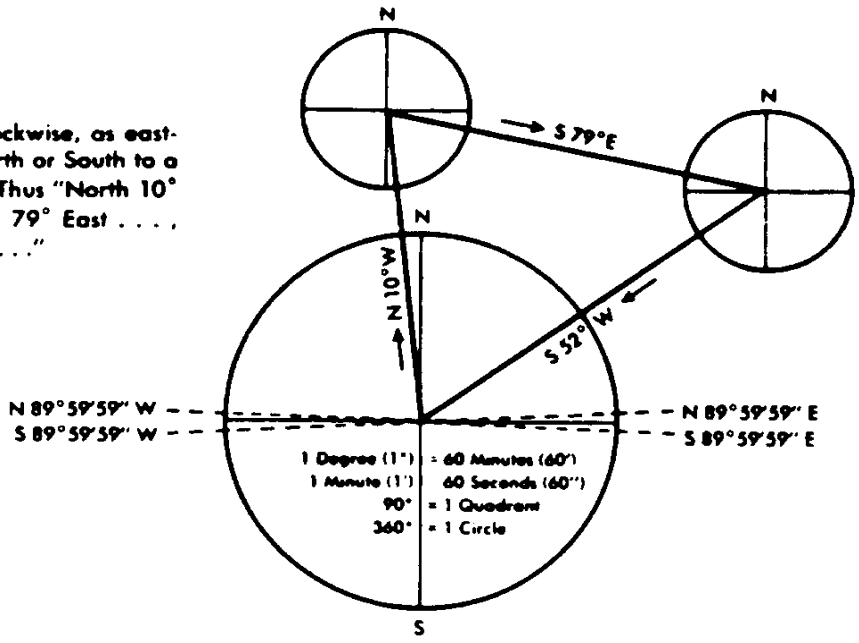
Figure 2 illustrates the meaning of descriptions by surveyors' courses. The bearing S 79° E indicates an angle 79 degrees to the east of due south; S 52° W indicates an angle 52 degrees to the west of due south; N 10° W indicates an angle 10 degrees west of due north. With this principle in mind, metes and bounds descriptions become understandable to many laymen. Computer programs are now available that will plot metes and bounds descriptions graphically, which is particularly useful to make sure that a description "closes" at the point of beginning.

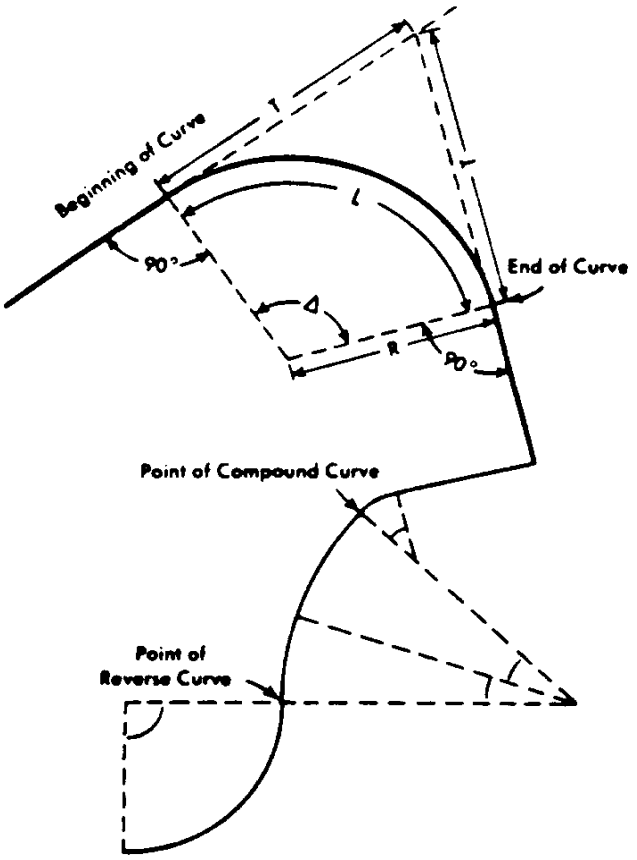
Print

Metes and Bounds

BEARINGS

Are given, commonly clockwise, as easterly or westerly from North or South to a maximum of 89°59'59". Thus "North 10° West . . . , thence South 79° East . . . , thence South 52° West . . . ."





CURVES

Simple, compound, or reverse, are analyzed and described as arcs of specified circles. Thus ". . . thence along a tangent curve to the right having a radius of 50 feet, through an angle of 120 degrees, an arc length of 104.72 feet" or R = 50', Δ = 120°, L = 104.72'.

FIGURE 2

© The Regents of the University of California

§11.33 b. General Courses

Occasionally, instead of presenting bearings and degrees, general courses, usually to a known point or monument, may be used. These are general compass directions that are typically used to refer to any line that lies within 20 degrees on either side of the direction used; *i.e.,* "easterly" would refer to anything between 20° north and 20° south of true east (or north 70° east and south 70° east). In the absence of a known point, however, this method is too vague for use.

© The Regents of the University of California

§11.34 c. Curves

Curves can be more complex and are described by three elements: radius, angle, and arc length. A short radius indicates a tight curve, while a long radius indicates a shallow curve. The angle indicates the amount of change in direction (a full circle being 360°); thus, an angle of 90° means that the direction at the end of the curve will be at right angles to the direction at the beginning of the curve. The arc length supplies the actual distance traveled by the curve. The symbols R = 50', D = 120°, L = 104.72' indicate a curve with a radius of 50 feet, turning 120 degrees in direction, through an arc 104.72 feet long. (A curve is sometimes described in terms of the angle that equates to 100 feet of arc length. The larger the radius of the arc, the smaller the required angle; thus, a 1° curve has a radius of almost 5730 feet, a 2° curve has a radius of 5730 ÷ 2 = 2865 feet, and so on.)

In describing curves, certain terms are used. The distance is the linear measurement of the portion of the curve that makes up that course of the description. Concave or convex refers to the inside or outside of a curve. General direction will occasionally be inserted on references to curves to establish the direction of travel. A tangent is the point at which the radius of the curve makes an angle of 90° with the course. Curves can be complex, and qualified title officers or surveyors should be consulted if the description is crucial.

© The Regents of the University of California

§11.35 d. Use of Symbols and Written Descriptions

Although symbols for feet (′), inches (″), and degrees (°) are conventionally used on maps, title companies prefer written descriptions because symbols are easily misread or mistranscribed and their meaning is too easily lost if the document is damaged or poorly copied. For the same reasons, it is better to spell out minutes (′), seconds (″), and angle (D) in written descriptions. Spelling out directions instead of abbreviating them also avoids error; for example, copying machines sometimes make an N look like a W.

© The Regents of the University of California

§11.36 e. Monuments

The most important aspects of metes and bounds descriptions are (1) that the courses be accurate and precise and (2) that the description close. It is typical in many metes and bounds descriptions to see a phrase to the effect that, on the last course, a distance "more or less, to the point of beginning" is used. In such an event, the monument controls over the course itself and as a matter of law and practice the last course is subordinate to the correct distance to reach the monument and make the description close. CCP §2077. With respect to the monuments used to mark properties, coterminous owners are bound to maintain them under CC §841.

© The Regents of the University of California

§11.37 f. Measurements

The following measurements are commonly encountered in descriptions:

- 1 chain = 66 feet = 4 rods
- 1 rod = 16.5 feet = 1 pole
- 1 mile = 80 chains = 5280 feet
- 1 acre = 10 square chains = (1/640 of a square mile) = 43,560 square feet = 160 square rods
- 1 acre in square form = 208.71 feet on each side
- 1 vara (Spanish unit) = 2.781 feet

Distances are measured horizontally and without regard to height variations in the earth's surface. Thus, the distance in Figure 3 is measured as four feet.

Print

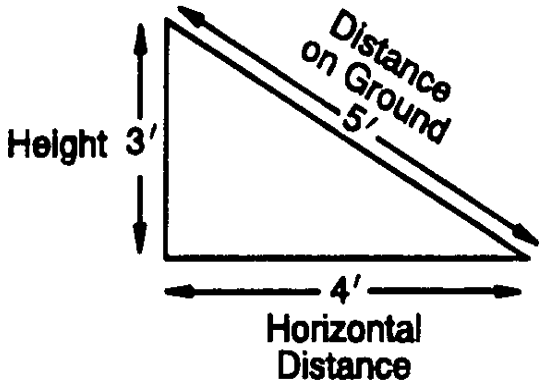


FIGURE 3

For further discussion, see Bowman & Milligan, Real Estate Law in California (10th ed 2000).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/11 Descriptions of Property/§11.38 7. Quasi Metes and Bounds

§11.38 7. Quasi Metes and Bounds

The following two examples illustrate a description by quasi metes and bounds.

EXAMPLE 1: This is a "strip" description:

> [A] strip of land extending easterly from Baker Road measuring 50 feet in width, the boundary lines of which are perpendicularly distant northerly 20 feet and southerly 30 feet, respectively, from the following described line….

EXAMPLE 2: This is a recital of boundaries by reference to matters of record, dimensions, or both:

> [B]eginning at the southeast corner of lot 6 in the map described above, then
> (a) Northeasterly to the West corner of land of Charles Abel per deed recorded at book 4, page 5, Official Records, office of County Recorder, Tulare County; then
> (b) Northeasterly along the northwest line of Charles Abel's land to the south line of Doe Lane as shown on subdivision map recorded at book 7, page 6 of Maps, Office of County Recorder of that county; then
> (c) 50 feet in a westerly direction along that south line; then
> (d) Southwesterly, parallel to the northwest line of Charles Abel's land to the south line of lot 6; then
> (e) Easterly to the point of beginning.

In each of these quasi metes and bounds descriptions, courses and distances are given, but the reference points are located by reference to deeds or maps rather than to physical monuments or surveyors' points.

In the strip description, the distance of the boundary lines is measured perpendicularly to the controlling line. This method prevents ambiguity that would result if the controlling line did not run due east and west. (In that situation, measuring 20 and 30 feet respectively due north and south would result in a strip less than 50 feet wide, as shown in Figure 4.)

Print

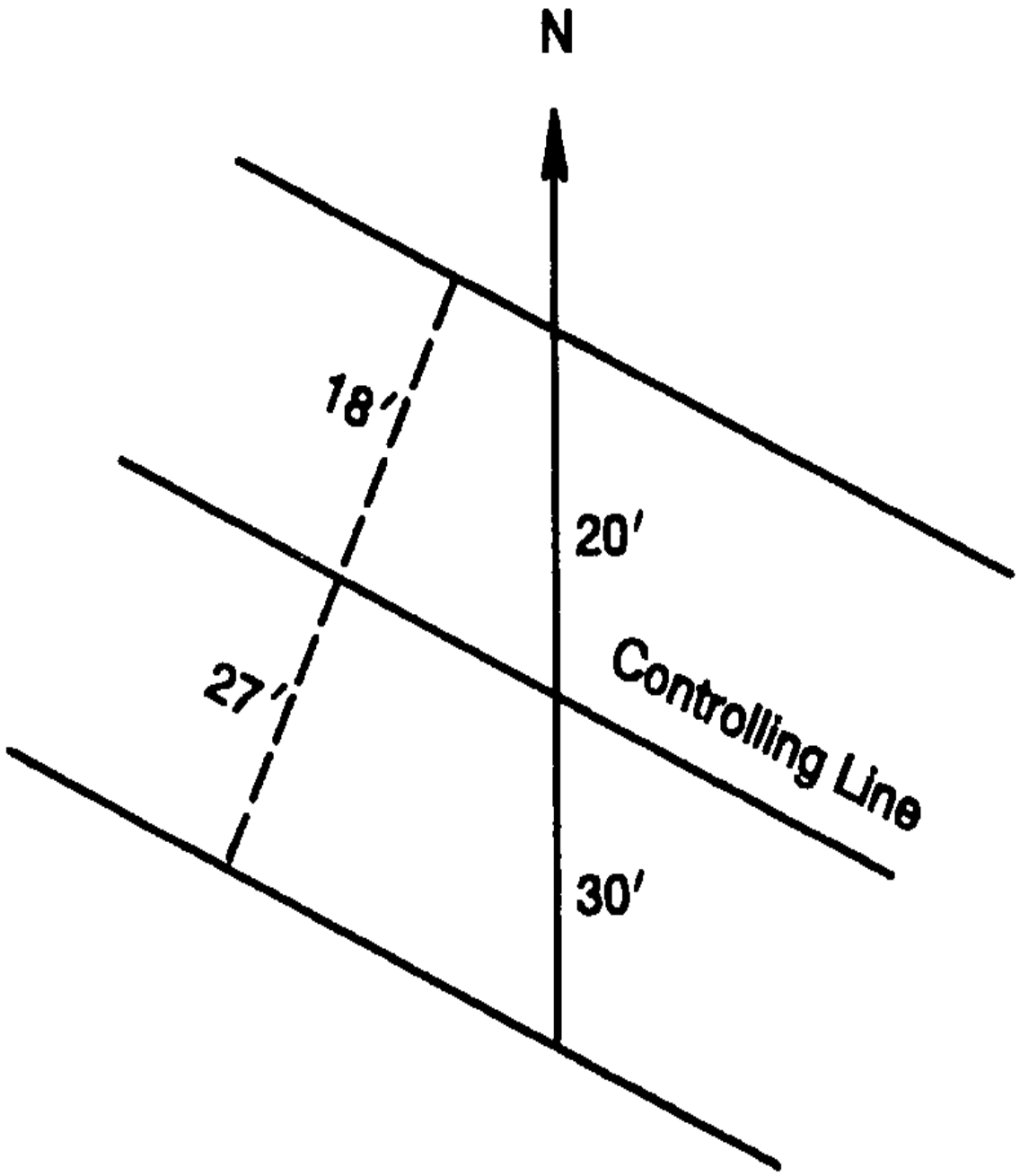


FIGURE 4

Similar problems arise from descriptions referring to, *e.g.,* the "north half" of an irregularly shaped lot. See §11.40.

© The Regents of the University of California

§11.39 8. Designation of North

The most commonly used designations of "north" are the following:

- **Grid**. The direction of grid north lies along a straight line between the two geographic poles. The north-south lines of the United States rectangular survey system indicate grid north.
- **Magnetic**. Magnetic north shifts about the geographic pole and is only intermittently in line with grid or astronomic north. Because of this shift, plats based on it should bear a date. See Brown, Robillard, & Wilson, Evidence and Procedures for Boundary Location (3d ed 1994).
- **Astronomic**. Astronomic north also shifts, but much more slowly (see Brown, Robillard, & Wilson). It is common in survey-located descriptions.

If plats or maps indicate which designation of north is used and is included in the recorded document containing the description, north need not be further identified in the description itself. The same is true of descriptions that refer to other recorded maps. Otherwise, the description should clearly state which designation of north is used.

© The Regents of the University of California

§11.40 I. Lot Division Description

Lot division description (so called because it is a means of dividing a lot or other parcel shown on a recorded map) is an apparently simple method of description, but the simplicity may be illusory. "The east half of Lot 7," may seem clear until it is discovered that Lot 7 is not a perfect rectangle. See example in Figure 5. Then the question arises whether "the east half" means half of the area or half of the width.

Print

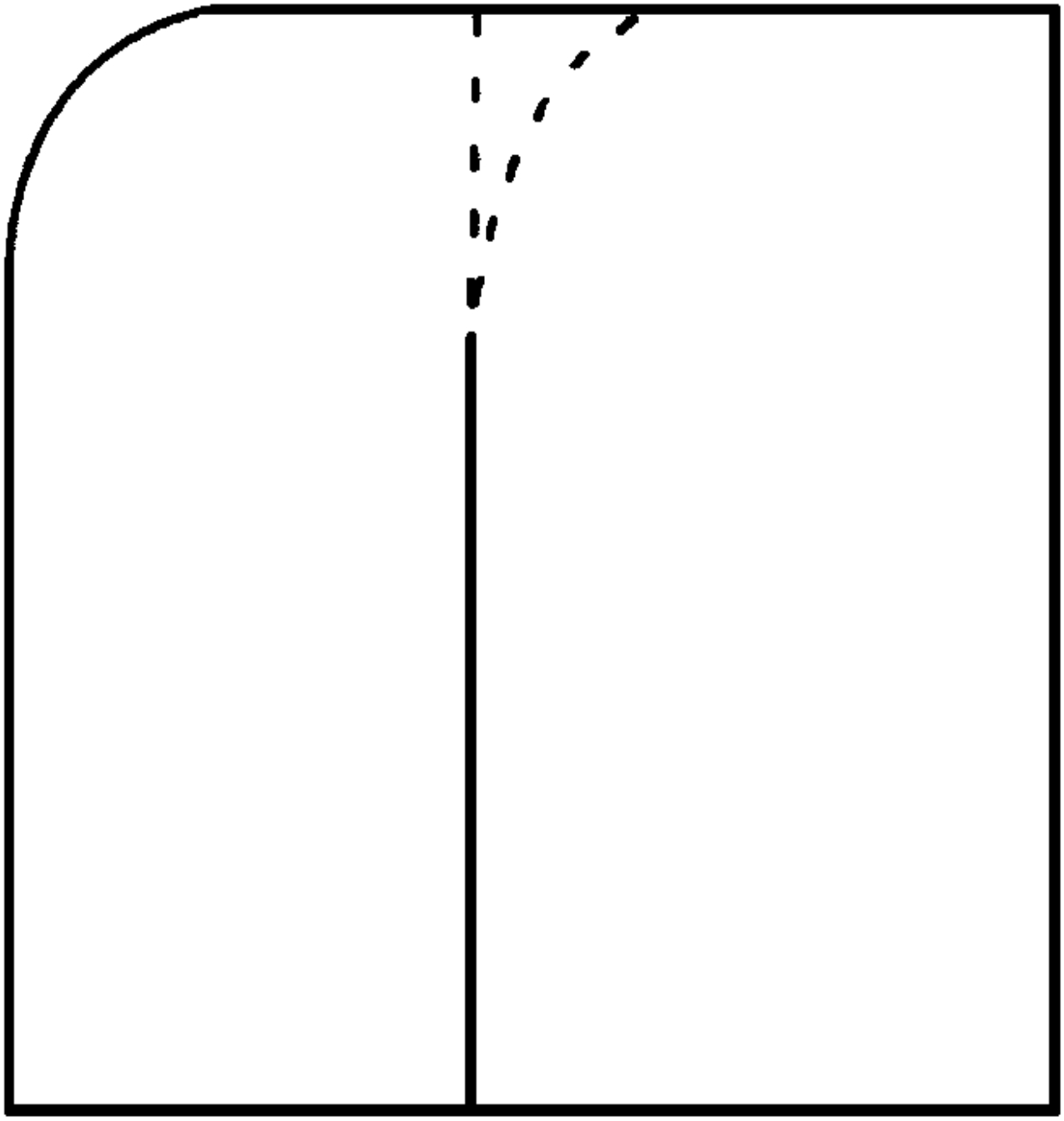


FIGURE 5

Similarly, "the south 50 acres of Lot 8" is ambiguous unless the original parcel is a rectangle whose boundaries run due north, south, east, and west. If not (see Figure 6), the question arises whether the fraction transferred was

intended to be a rectangle occupying the more or less southerly 50 acres or an irregular parcel of 50 acres with its northern line running due east and west. See Figure 4 in §11.38 for a discussion of the problem.

Print

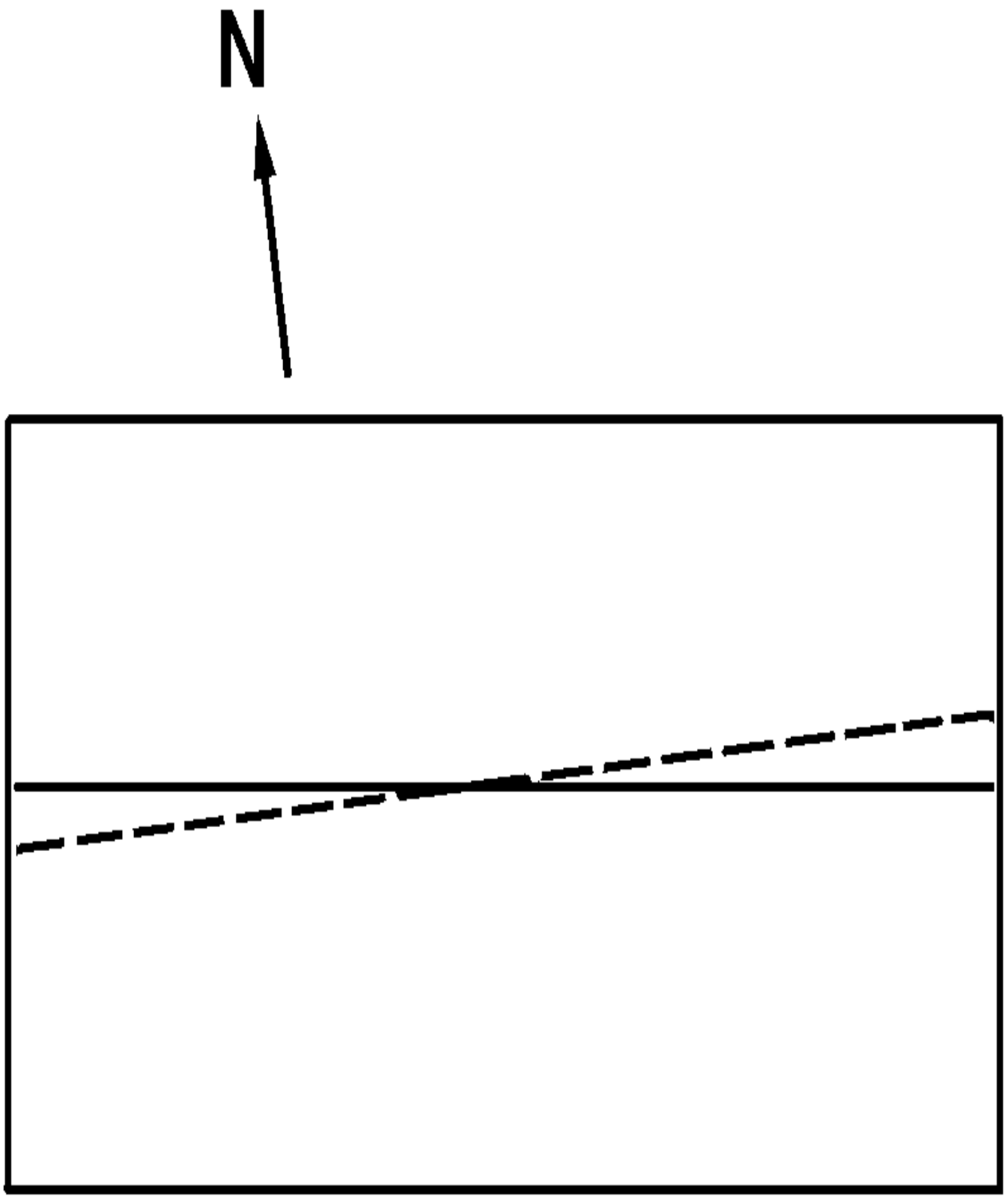


FIGURE 6

In the example shown in Figure 7, is the "northerly 50 feet of Lot 9" to be measured along the 100-foot frontage on the street or across the 90-foot width?

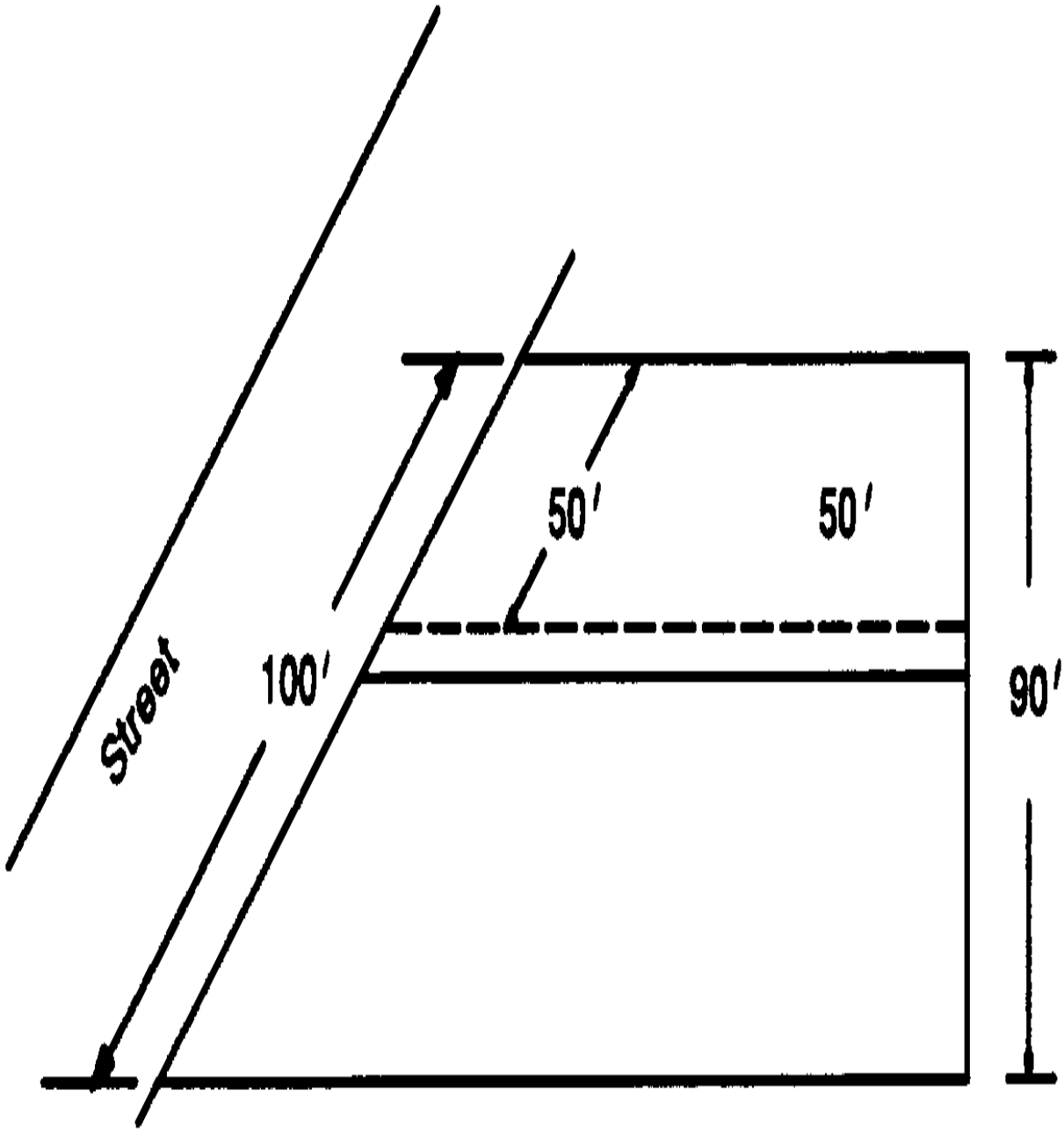


FIGURE 7

To avoid litigation and the frustration of intent that may result from these ambiguities, lawyers for sellers as well as for buyers should insist on absolute clarity in the description. Here are some guidelines:

- Avoid fractional descriptions unless they are clarified by metes and bounds or by a clear statement of how to measure the fractional parts.
- Specify the directions of all measurements, bearing in mind the discussion in §11.39 on indicating direction.
- Supplement all descriptions of area with clear descriptions of boundaries and location.
- If the parcel adjoins a street or a road (particularly if any measurement is from or along the street or road), declare whether the grantor's interest, if any, in the road is included, and whether the measurement is from or along the center or the edge of the road. See §11.30. See Figure 8 for an example of the difference this could make. On counseling the seller on lot splits, see §1.31.



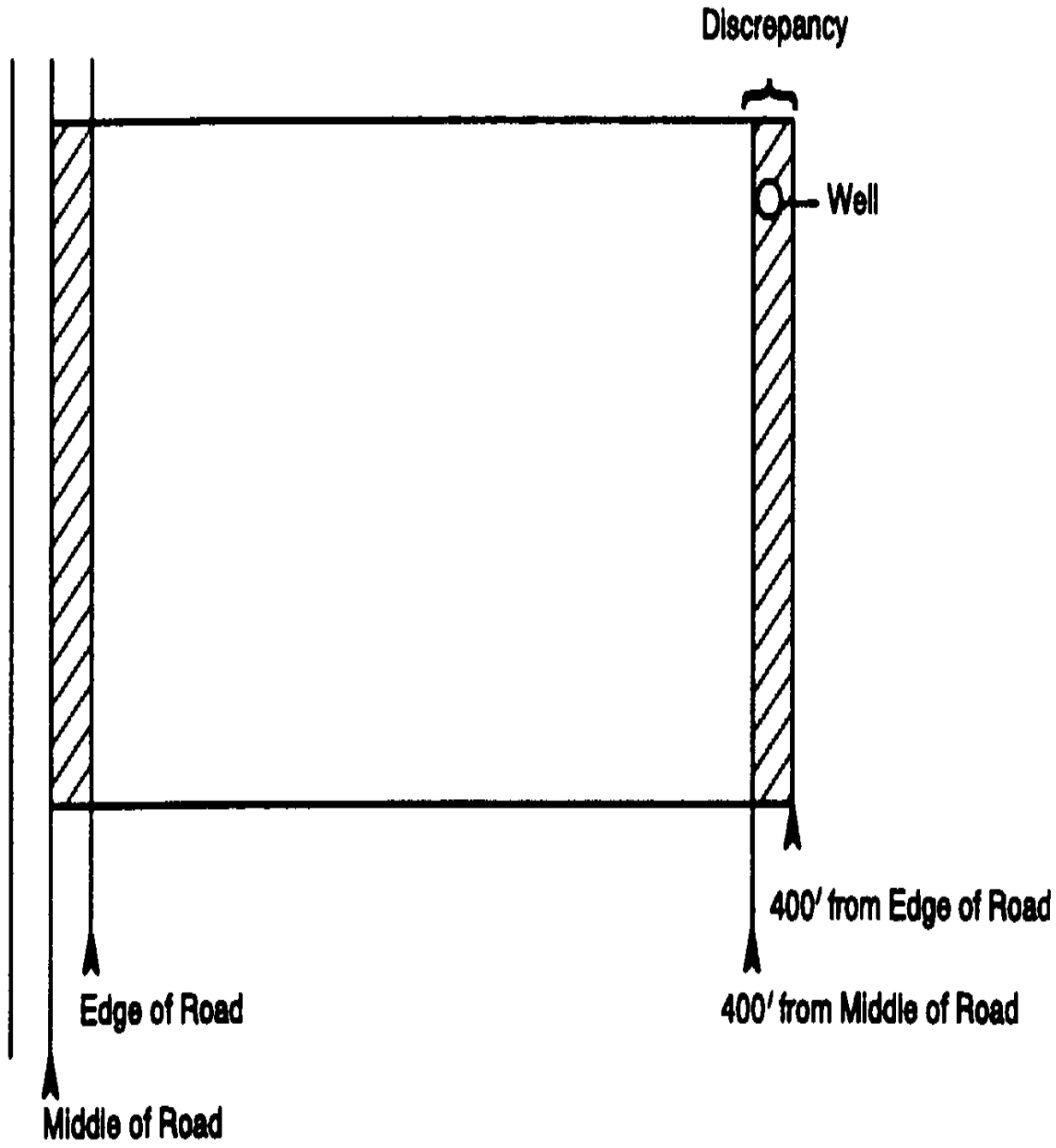


FIGURE 8

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/11 Descriptions of Property/§11.41 J. General or Common Description

§11.41 J. General or Common Description

General descriptions are divided into five types:

- A blanket description ("all the lands belonging to the grantor in Black County");
- A description of all "unsold" or "unconveyed" lots of the grantor;
- A description by name ("all of Blackacre");
- A description by street number ("159 South Lincoln Street"); and
- A description by ownership ("my lot in Shasta County").

Each of these descriptions presents problems of proof. On proper evidence, many of them have been sustained but none can be supported as examples of acceptable drafting because more precise descriptions are possible.

© The Regents of the University of California

IV. MATTERS ALTERING OR AFFECTING DESCRIPTIONS

§11.42 A. Effect on Record Title

Matters outside the record may substantially affect title and may either augment or diminish the estate. Examples are in §§11.54-11.67, 11.71, and 11.77-11.79 and may not appear in preliminary reports unless they have previously been established by judgments.

A lawyer reading a description in order to advise a client on its effect cannot give an adequate opinion without investigating the existence and effect of any off-record elements.

© The Regents of the University of California

B. Easements

§11.43 1. Benefit and Burden

Property subject to or burdened by an easement is called the "servient tenement"; the property benefited by or to which the easement is attached is the dominant tenement. CC §803. An easement is a nonpossessory interest in the land of another, which entitles the owner of the easement to a limited use or enjoyment of the other's land. *Kazi v State Farm Fire & Cas. Co.* (2000) 24 C4th 871, 880, 103 CR2d 1; *Reichardt v Hoffman* (1997) 52 CA4th 754, 767, 60 CR2d 770. Restatement (Third) of Property: Servitudes §1.2 (2000); 12 Witkin, Summary of California Law, *Real Property* §§382-428 (10th ed 2005). Because an easement is a nonpossessory interest in real property, it is never an "estate in land." *Hubbard v Brown* (1990) 50 C3d 189, 194, 266 CR 491; *Darr v Lone Star Indus., Inc.* (1979) 94 CA3d 895, 901, 157 CR 90 (superseded by statute on other grounds).

When an easement is nonexclusive, the common users must accommodate each other. *Reichardt v Hoffman, supra*; *Scruby v Vintage Grapevine, Inc.* (1995) 37 CA4th 697, 43 CR2d 810. The owner of the dominant tenement must use his or her easements and rights in such a way as to impose as slight a burden as possible on the servient tenement. *Locklin v City of Lafayette* (1994) 7 C4th 327, 356 n17, 27 CR2d 613; *Reichardt v Hoffman, supra*. The owner of the servient tenement may use the burdened land in any way that does not interfere unreasonably with the use of the easement. *Camp Meeker Water Sys., Inc. v Public Util. Comm'n* (1990) 51 C3d 845, 274 CR 678; *Scruby v Vintage Grapevine, Inc., supra*.

When an easement is nonexclusive, the common owners must accommodate each other. *Reichardt v Hoffman, supra*; *Scruby v Vintage Grapevine, Inc., supra*.

Easements must be used in accordance with applicable zoning restrictions, notwithstanding any private agreement to the contrary. *Teachers Ins. & Annuity Ass'n v Furlotti* (1999) 70 CA4th 1487, 83 CR2d 455. On easements generally, see California Easements and Boundaries: Law and Litigation (Cal CEB 2008).

© The Regents of the University of California

§11.44 2. Rules of Construction and Interpretation

Descriptions of easements are subject to a number of rules of construction and interpretation. The rules can be particularly important in ascertaining (1) what easements a parcel of land may be subject to and (2) whether a parcel is adequately supported by easements necessary for the use contemplated by the owner or developer. It is important, as part of due diligence, to review the width and set-back requirements applicable to the use of easements or placement of improvements under local land use controls. On rules of construction, see California Easements and Boundaries: Law and Litigation, chap 1 (Cal CEB 2008).

© The Regents of the University of California

§11.45 a. Limitation to Use of Specified Width

A grant of an easement is usually construed literally. In *Ballard v Titus* (1910) 157 C 673, 680, 110 P 118, the grant of a 30-foot wide easement limited the grantee strictly to the strip for all purposes, including embankments for a road. The court determined that when the width of a right-of-way is expressly specified, there is no authority for the appropriation of land lying beyond the specified width even though the appropriation may be necessary or desirable for appurtenant structures.

© The Regents of the University of California

§11.46 b. Right to the Use of Streets and Alleys Reflected on Subdivision Map

Conveyance of a lot by a deed that refers to a map makes the map part of the deed. If the map shows streets and alleys, a reference to the map is considered equivalent to a declaration that a right to use these passageways is attached to each lot as an appurtenance. *Danielson v Sykes* (1910) 157 C 686, 689, 109 P 87; *Tract Dev. Servs., Inc. v Kepler* (1988) 199 CA3d 1374, 1382, 246 CR 469. The rule applies regardless of whether a city or county has ever accepted a dedication of the rights-of-way laid out on the map or whether the rights-of-way have ever been opened or used. These rights cannot be divested except by due process of law. *Danielson v Sykes, supra*.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/11 Descriptions of Property/§11.47 c. Inclusion of Rights for Utilities

§11.47 c. Inclusion of Rights for Utilities

A grant of an easement for ingress and egress does not grant a right for utilities. See *San Rafael Ranch Co. v Ralph Rogers Co.* (1908) 154 C 76, 96 P 1092.

NOTE: Easements for utilities can be acquired under CC §1001.

© The Regents of the University of California

§11.48 d. Doctrine of Practical Location and Amendment of Written Descriptions by Actual Location

Some cases have recognized a doctrine of "practical location," which provides that delineation of parcels on the ground by fixed monuments, relied on by the parties, will control over any differing description in the deed. *French v Brinkman* (1963) 60 C2d 547, 1551, 35 CR 289. In *PG&E v Minnette* (1953) 115 CA2d 698, 704, 252 P2d 642, it was held that set monument stakes, fixing the location on the ground and acquiesced in by the parties, would control any technical construction of the description in the deeds. The court reached this result under the rule that the acts of the parties afford the most reliable evidence of their actual intention.

NOTE: A buyer may be charged with constructive notice of any lack of conformity between the written description and the actual location of the easement by inspection of the land. CC §19.

© The Regents of the University of California

§11.49 e. Interpretation by Language of the Document and Extrinsic Evidence

Grants are to be interpreted in the same way as contracts in general. CC §1066; *Continental Baking Co. v Katz* (1968) 68 C2d 512, 521, 67 CR 761. The primary object of interpretation is to ascertain and carry out the intention of the parties. All rules of interpretation must be considered and each given its proper weight to arrive at the true effect of the instrument. *City of Manhattan Beach v Superior Court* (1996) 13 C4th 232, 238, 52 CR2d 82; *Machado v Southern Pac. Transp. Co*. (1991) 233 CA3d 347, 352, 284 CR 560. This is accomplished by resorting first to the language of the document. If the deed is susceptible to only one interpretation, a court will decline to consider extrinsic evidence. *Severns v Union Pac. R.R. Co.* (2002) 101 CA4th 1209, 1214, 125 CR2d 100; *City & County of San Francisco v Union Pac. R.R. Co.* (1996) 50 CA4th 987, 994, 58 CR2d 1; *Concord & Bay Point Land Co. v City of Concord* (1991) 229 CA3d 289, 294, 280 CR 623. Extrinsic evidence is admissible to interpret the instrument, but not to give it a meaning to which it is not susceptible. It is the instrument itself that must be given effect. See *Claudino v Pereira* (2008) 165 CA4th 1282, 1288, 82 CR3d 464 (aggregate legal description, which included townsite map and surveyor's field notes, was ambiguous; extrinsic evidence admitted to resolve ambiguity in field notes); *City of Manhattan Beach v Superior Court, supra,* citing *Parsons v Bristol Dev. Co.* (1965) 62 C2d 861, 865, 44 CR 767; *Buehler v Oregon-Washington Plywood Corp.* (1976) 17 C3d 520, 528, 131 CR 394 (extrinsic evidence was admitted to clarify scope of dominant tenement).

© The Regents of the University of California

§11.50 f. Accommodation of Future Needs

Because the operation of an easement must necessarily be prospective, in the case of easements created by express conveyance it can be assumed that the parties intended to accommodate future needs. Changes in use through modernization of facilities, such as from street railways to modern buses and roadways, have been upheld. *Faus v City of Los Angeles* (1967) 67 C2d 350, 355, 62 CR 193. See also *Anderson v TimeWarner Telecom* (2005) 129 CA4th 411, 415, 28 CR3d 289 (fiber optic facilities held consistent with telegraph and telephone provisions of Pub Util C §7901 applicable to county right-of-way); *Bello v ABA Energy Corp.* (2004) 121 CA4th 301, 16 CR3d 818 (gas pipeline held permissible in public right-of-way). The doctrine is strictly limited to use of the original right-of-way in the same, but not a different, location. *Faus,* 67 C2d at 359. Changes in use inconsistent with the purpose of the grant are not permitted. *Toews v U.S.* (2004) 376 F3d 1371, 1379 (rejecting conversion of railroad easement to pedestrian use under Rails to Trails Act).

© The Regents of the University of California

§11.51 g. Exercise of General Grant of Easement in a Particular Course or Manner

The rule is well settled that when a grant of easement is general concerning the extent of the burden to be imposed on the servient tenement, an exercise of the right with the acquiescence and consent of the parties in a particular course and manner fixes the easement and limits it to the particular location and scope in which it is enjoyed. *Winslow v City of Vallejo* (1906) 148 C 723, 725, 84 P 191. Once fixed, it cannot be changed without consent.

© The Regents of the University of California

§11.52 h. Exclusivity of Easements

An exclusive easement is an unusual interest in land and has been said to amount almost to conveyance of a fee. *Pasadena v California-Michigan* (1941) 17 C2d 576, 578, 110 P2d 983. No intention to convey an exclusive easement will be imputed in the absence of clear evidence of such an intention. *Pasadena v California-Michigan, supra*; *Mehdizadeh v Mincer* (1996) 46 CA4th 1296, 1308, 54 CR2d 284. In *Blackmore v Powell* (2007) 150 CA4th 1593, 1600, 59 CR3d 527, an easement for parking and garage purposes was upheld notwithstanding the exclusivity of the use. See *Gray v McCormick* (2009) 167 CA4th 1019, 84 CR3d 777 (exclusive easement language contained in subdivision CC&Rs held enforceable as to surface of land).

© The Regents of the University of California

§11.53 3. Off-Record Easements

Examination of the record alone is insufficient for discovering an easement, because easements may be created by means not shown on the record. This possibility emphasizes the need to inspect the parcel to ascertain whether any easements exist or may come into being. Some of the off-record easements that may arise are discussed in §§11.54-11.57 and 11.77-11.79.

© The Regents of the University of California

§11.54 a. Easements by Implication

Civil Code §1104 provides that a transfer of real property passes all easements attached to the property and creates an easement to use other real property of the person whose estate is transferred in the same manner and in the same extent as such property was obviously and permanently used. *Kytasty v Godwin* (1980) 102 CA3d 762, 771, 162 CR 556. An implied easement must be reasonably necessary to the use and benefit of the quasi-dominant tenement and will not be found absent clear evidence that it was intended by the parties. *Tusher v Gabrielsen* (1998) 68 CA4th 131, 141, 80 CR2d 126. The limiting factor is the obvious and permanent use at the time of the conveyance. The factors listed in §1104, however, are not exclusive of other common law factors applicable in certain situations.

If the parties to a transaction intend a greater extent of the grantee's rights, that intent will be recognized by the court. *Fristoe v Drapeau* (1950) 35 C2d 5, 9, 215 P2d 729; *Sierra Screw Prods. v Azusa Greens, Inc*. (1979) 88 CA3d 358, 368, 151 CR 799; *Horowitz v Noble* (1978) 79 CA3d 120, 133, 144 CR 710. The distinction in this group of cases is that the courts will enforce the intent of the parties to a particular transaction, whereas implications by code depend on obvious and permanent use—in effect, equivalent to notice imparted by possession or a duty of inquiry. In the absence of obvious and permanent use or facts triggering a duty of inquiry, a bona fide third party grantee is entitled to the protection of the recording laws. CC §§1169-1172, 1206-1218. On easements by implication, see California Easements and Boundaries: Law and Litigation, chap 1 (Cal CEB 2008).

© The Regents of the University of California

§11.55 b. Easements by Implied Reservation

Just as an easement may arise by implication for the buyer's benefit, it may arise to the buyer's detriment. *Horowitz v Noble* (1978) 79 CA3d 120, 133, 144 CR 710. Although an easement is less readily implied in favor of a grantor (*Jordan v Henck* (1958) 166 CA2d 321, 325, 333 P2d 117), a sale of a portion of land with irrigation ditches on it imposes a burden on the buyer to permit the water to flow through the ditches to the land retained by the seller (*Palvutzian v Terkanian* (1920) 47 CA 47, 190 P 503). The preexisting use by the grantor must be open, visible, and continuous at the time of the conveyance. *People v Bowers* (1964) 226 CA2d 463, 38 CR 238. See also California Easements and Boundaries: Law and Litigation, chaps 1, 8 (Cal CEB 2008).

© The Regents of the University of California

§11.56 c. Easement of Necessity

Unlike an implied easement under CC §1104, an easement of necessity does not depend on prior use but arises by operation of law. If at the time of the conveyance the dominant and servient tenements are owned by the same person and there is an absolute necessity for the easement because it is the only access (*e.g.,* when the land sold is otherwise landlocked), an easement of necessity is created. See *Murphy v Burch* (2009) 46 C4th 157, 162, 92 CR3d 381; *Kellogg v Garcia* (2002) 102 CA4th 796, 803, 125 CR2d 817. Availability of other access at the time of the conveyance bars an easement of necessity over more convenient access (*Reese v Borghi* (1963) 216 CA2d 324, 30 CR 868), and if other access later becomes available so that the necessity disappears, the easement ceases (*Irvin v Petitfils* (1941) 44 CA2d 496, 112 P2d 688). The "strict necessity" element must continue to exist at the time of the action. In *Moores v Walsh* (1995) 38 CA4th 1046, 45 CR2d 389, an owner of the dominant tenement was denied an easement by necessity because the dominant tenement had been sold to the tenant by the state after the original division of the dominant and servient tenements. The state thus could have acquired the easement by eminent domain, but had not; therefore, the necessity for the easement had not continually existed until the time of the plaintiff's purchase.

The doctrine has been applied to an implied reservation of an easement for the benefit of landlocked property conveyed by the federal government. *Kellogg v Garcia* (2002) 102 CA4th 796, 804, 125 CR2d 817. However, the easement claimant bears the burden of producing evidence to overcome the inference caused by omission of an express reservation of a right of access to property initially retained by the government. See *Murphy v Burch* (2009) 46 C4th 157, 167, 92 CR3d 381 (government sold parcel without reserving access rights, leaving its remaining parcel, landlocked).

The easement's use is limited by the necessity for the easement itself. The common-ownership requirement for creation of an easement of necessity can be met even if the ownership of one parcel is only an equitable title at the time of the conveyance. *Roemer v Pappas* (1988) 203 CA3d 201, 249 CR 743 (equitable title acquired under an installment land sale contract). In *Noronha v Stewart* (1988) 199 CA3d 485, 245 CR 94, the court held that an agreement to grant the equivalent of an easement was binding even though the owner of property on which a wall was built held only equitable title at the time the license was granted, although the owner did acquire legal title later. The court held that the doctrine of "after-acquired title" applied to overcome the technicality that the original owner did not have a sufficient interest in the property to grant the easement at the time it was granted. On easements by necessity, see California Easements and Boundaries: Law and Litigation, chap 1 (Cal CEB 2008).

© The Regents of the University of California

§11.57 d. Easement by Prescription

California law recognizes two types of prescription, that under claim of title (CCP §§322-323) and that under claim of right (CCP §§324-325). *Gilardi v Hallam* (1981) 30 C3d 317, 321, 178 CR 624. The elements necessary to establish a prescriptive easement under either claim of title or claim of right are open and notorious use or possession that is continuous and uninterrupted, and that is hostile to the true owner under a claim of title or right, for at least 5 years. Taxes are an element of the acquisition of a prescriptive easement only if the easement was separately assessed. *Gilardi v Hallam, supra*.

A prescriptive easement cannot arise if the use occurs with the owner's permission or if it is an easement of necessity (see §11.56), flowing from the grant and the circumstances then existing.

A prescriptive easement may not be granted if doing so would result in depriving the owner of essentially all rights in the property; in that case, the claimant must proceed under the adverse possession doctrine and show payment of taxes on the disputed property. *Kapner v Meadowlark Ranch Ass'n* (2004) 116 CA4th 1182, 1186, 11 CR3d 138; *Harrison v Welch* (2004) 116 CA4th 1084, 11 CR3d 92; *Bustillos v Murphy* (2002) 96 CA4th 1277, 117 CR2d 895; *Silacci v Abrahamson* (1996) 45 CA4th 558, 53 CR2d 37.

The rule that the use of a prescriptive easement is fixed and determined by the manner of use in which it originated, and that it cannot be extended or increased, has been modified to allow such increased use if the change is one of degree, not kind. In deciding whether a particular use is permissible under such an easement, the courts may consider the needs that result from the normal development in the use of the dominant tenement as well as the increased burden on the servient tenement. *Applegate v Ota* (1983) 146 CA3d 702, 711, 194 CR 331; *Cushman v Davis* (1978) 80 CA3d 731, 145 CR 791. Any claim for the expansion of easement rights must be exercised openly, notoriously, continuously, and adversely during the period of prescription. *Security Pac. Nat'l Bank v City of San Diego* (1971) 19 CA3d 421, 97 CR 61. For the fee owner's authority to post notice of permission, which precludes prescriptive easements, see CC §1008. See §11.77 on adverse possession, prescription, and implied dedication.

Easements may not be acquired by prescription over property dedicated to a public utility or a public entity. CC §1007. In *Hays v Vanek* (1989) 217 CA3d 271, 266 CR 856, a road offered but not accepted for dedication to the county was nonetheless held to be quasi-public to a degree sufficient to prevent adverse possession under §1007. Within narrow guidelines, a court has the equitable power to allow a continuing encroachment that may be limited in scope and duration. *Hirshfield v Schwartz* (2001) 91 CA4th 749, 110 CR2d 861; see also *Linthicum v Butterfield* (2009) 175 CA4th 259, 265, 95 CR3d 538 (court recognized historic road, but limited width of right of way to that reasonably necessary). On easements by prescription, see California Easements and Boundaries: Law and Litigation, chap 1 (Cal CEB 2008).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/11 Descriptions of Property/§11.58 4. Termination of Easements

§11.58 4. Termination of Easements

Easements may exist on or off the record; they may also be terminated by means that may or may not appear on the record. CC §811. Easements may be terminated by the following events:

- Merger (see §11.59);
- Destruction of the servient tenement (see §11.60);
- Incompatible use or misuse (see §11.61);
- Abandonment (see §11.62);
- Nonuse of prescriptive easements (see §11.63); and
- Adverse possession (see §11.64).

© The Regents of the University of California

§11.59 a. Termination by Merger

If the dominant and servient parcels come into the same ownership, the easement is extinguished by merger. CC §811(1). The doctrine of merger requires that the two estates be coextensive in validity, quality, and all other circumstances of right. *Zanelli v McGrath* (2008) 166 CA4th 615, 628, 82 CR3d 835. For an easement to be extinguished, the ownership must be of the entire dominant and servient tenements and not merely a fractional share. 166 CA4th at 629. However, equity will intervene to prevent or permit a merger of interests, as will best serve the purposes of justice, and the actual and just intent of the parties. *Ito v Schiller* (1931) 213 C 632, 635, 3 P2d 1. On termination by merger, see California Easements and Boundaries: Law and Litigation, chap 1 (Cal CEB 2008).

© The Regents of the University of California

§11.60 b. Termination by Destruction of Servient Tenement

An easement, typically one on or through improvements such as buildings, is terminated when the servient tenement is destroyed (CC §811(2)) either involuntarily by fire (*Cohen v Adolph Kutner Co*. (1918) 177 C 592, 171 P 424), or through demolition after obsolescence (*Walner v City of Turlock* (1964) 230 CA2d 399, 41 CR 29). In *Fletcher v Stapleton* (1932) 123 CA 133, 10 P2d 1019, this doctrine also applied to a graded property where an original right-of-way no longer had practical utility, and another more convenient way had been acquired. On termination by destruction or other changed conditions, see California Easements and Boundaries: Law and Litigation, chap 1 (Cal CEB 2008).

© The Regents of the University of California

§11.61 c. Termination by Incompatible Use or Misuse

An easement may be extinguished by its owner's acts, or assent to acts, that are incompatible with the nature or exercise of the easement. CC §811(3). See, *e.g., Crimmins v Gould* (1957) 149 CA2d 383, 308 P2d 786 (extinguishment by greatly increasing burden and opening private easement to public).

NOTE: If the holder of a nonexclusive easement prevents the burdened property owner from using the easement, the owner's remedy is not extinguishment of the easement but an injunction requiring the holder to permit the burdened property owner's use of the easement. *Reichardt v Hoffman* (1997) 52 CA4th 754, 60 CR2d 770.

On termination by misuse, see California Easements and Boundaries: Law and Litigation, chap 1 (Cal CEB 2008).

© The Regents of the University of California

§11.62 d. Termination by Abandonment

When an easement has been acquired by grant, the mere nonuse, neglect, or failure to maintain the easement does not result in abandonment. An intention to abandon by the holder of an easement must be clearly established by unequivocal and decisive acts on the part of the dominant tenement clearly showing an intention to abandon. *Gerhard v Stephens* (1968) 68 C2d 864, 882, 69 CR 612; *Tract Dev. Servs., Inc. v Kepler* (1988) 199 CA3d 1374, 1384, 246 CR 469; *Buechner v Jonas* (1964) 228 CA2d 127, 39 CR 298.

A servitude is extinguished by performance of an act by the servitude's owner, or with the owner's assent, that is incompatible with the servitude's nature or exercise. CC §811. To constitute an extinguishment, the act should be of a nature that would permanently prevent the easement's use, and be of a character to indicate a clear intent to abandon. *Reichardt v Hoffman* (1997) 52 CA4th 754, 60 CR2d 770.

An easement acquired by a utility for a public purpose is terminated by abandonment of that purpose. *People v Ocean Shore R.R.* (1948) 32 C2d 406, 417, 196 P2d 570; *Slater v Shell Oil Co.* (1940) 39 CA2d 535, 549, 3 CR 697. An easement is also terminated by nonuse coupled with acts by the owner that are inconsistent with further enjoyment of the right. *Ocean Shore R.R. Co. v Doelger* (1960) 179 CA2d 222, 231, 3 CR 706; *Flanagan v San Marco Silt Co.* (1951) 106 CA2d 458, 464, 235 P2d 107. On termination by abandonment, see California Easements and Boundaries: Law and Litigation, chap 1 (Cal CEB 2008).

© The Regents of the University of California

§11.63 e. Termination by Nonuse of Easements Acquired by Prescription

An easement by prescription (see §11.57) is extinguished by nonuse for the prescriptive 5-year period. CC §811(4); *People v Ocean Shore R.R*. (1948) 32 C2d 406, 419, 196 P2d 570; *Zimmer v Dykstra* (1974) 39 CA3d 422, 434, 114 CR 380.

© The Regents of the University of California

§11.64 f. Termination by Adverse Possession

Just as an easement may be acquired by prescription (see §11.57), it may likewise be terminated by the adverse possession of the owner of the servient tenement. In *Glatts v Henson* (1948) 31 C2d 368, 188 P2d 745, the owner of the servient tenement erected a building on the part of his lot that had an easement on it for road purposes; the buildings remained undisturbed for more than 5 years. The part of the easement on which the building stood was held extinguished. See also *Masin v La Marche* (1982) 136 CA3d 687, 186 CR 619. On termination by prescription, see California Easements and Boundaries: Law and Litigation, chap 1 (Cal CEB 2008).

© The Regents of the University of California

§11.65 5. Identification of Dominant Tenement

Though an easement may be of record, it may not show on its face the dominant tenement other than by reference to the grantee because the easement encumbers the servient property of record, not the dominant property. A search of the chain of title of nearby parcels may be needed to identify the dominant tenement(s). If the dominant tenement has since been subdivided, there may be many parcels with a claim to use of the easement, each of which could be a cloud on the title of the servient tenement.

Parol evidence is admissible to show what land composes the dominant tenement. In *Continental Baking Co. v Katz* (1968) 68 C2d 512, 67 CR 761, the supreme court rejected the servient owner's contention that, because a deed conveyed one parcel plus an easement over an adjacent parcel, the benefit of the easement was limited to the parcel conveyed. Instead, the court permitted the dominant tenant to offer parol proof that other adjacent land owned by him was also intended to share the benefit of the easement. See also *Welch v Kai* (1970) 4 CA3d 374, 84 CR 619.

A common law rule that no easement could be reserved in a stranger was abolished by the decision in *Willard v First Church of Christ, Scientist* (1972) 7 C3d 473, 102 CR 739. The court held that, because there had been no reliance on the old rule, the doctrine could not be used to defeat the grantor's intent. Thus, the dominant tenement of an easement created by reservation need no longer be land held by the grantor. On dominant tenements, see California Easements and Boundaries: Law and Litigation, chap 1 (Cal CEB 2008).

© The Regents of the University of California

§11.66 6. Change in Burden on Servient Tenement

Traditionally, once an easement has been established by prescription, the scope of that easement is fixed. *Bartholomew v Staheli* (1948) 86 CA2d 844, 195 P2d 824. The dominant owner cannot thereafter materially increase the burden on the servient tenement, impose new kinds of uses on the easement, or do anything that interferes with the servient owners' use of the property. *Durfee v Garvey* (1889) 78 C 546, 551, 21 P 302; *Baker v Pierce* (1950) 100 CA2d 224, 226, 223 P2d 286; *Joseph v Ager* (1895) 108 C 517, 41 P 422. More recent cases, however, have adopted the Restatement of Property position that a limited reasonable expansion in the normal evolution of the use can be considered if the burden on the servient tenement is not unreasonably increased. *Cushman v Davis* (1978) 80 CA3d 731, 736, 145 CR 791; *Gaither v Gaither* (1958) 165 CA2d 782, 332 P2d 436. If the increased burden is reasonably foreseeable, then the court must consider whether it constitutes normal development "consistent with the pattern formed by the adverse use by which the prescriptive easement was created." *Hill v Allan* (1968) 259 CA2d 470, 484, 66 CR 676.

Gates or other restrictions may be allowable if necessary for use of the servient tenement, provided there is no unreasonable interference with passage and they are not otherwise inconsistent with the terms of the grant. *Van Klompenburg v Berghold* (2005) 126 CA4th 345, 350, 23 CR3d 799. On changes in burden of servient tenement, see California Easements and Boundaries: Law and Litigation, chap 1 (Cal CEB 2008).

© The Regents of the University of California

§11.67 7. Appurtenant or in Gross

One difficulty in advising clients on easements is the difference between "appurtenant" easements (which pass, to the extent they are obviously and permanently in use, with the fee to the dominant tenement, even if not mentioned in the conveyance) and easements "in gross" (which exist without a dominant tenement and cannot pass unless expressly transferred). If the easement was created to benefit the easement holder in using particular land, it is appurtenant. See Restatement (Third) of Property: Servitudes §1.5(1) (2000). If the easement was created independently of the holder's ownership or possession of any specific land, it is in gross. See Restatement §1.5(2). The types of easements that are appurtenant to land and those that are not are listed in CC §§801 and 802, respectively. On drafting to eliminate ambiguity in easements, see §§11.15, 11.89-11.103; Kratovil, *Easement Draftsmanship and Conveyancing*, 38 Calif L Rev 426, 437 (1950). On easements in gross, see California Easements and Boundaries: Law and Litigation, chap 1 (Cal CEB 2008).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/11 Descriptions of Property/§11.68 a. Distinguishing Characteristics

§11.68 a. Distinguishing Characteristics

The following considerations distinguish appurtenant easements from easements in gross:

- The nature of the right and the intention of the parties creating it are determinative of the kind of easement created. *Schofield v Bany* (1959) 175 CA2d 534, 346 P2d 891; *Eastman v Piper* (1924) 68 CA 554, 568, 229 P 1002.
- The right is not personal (in gross) if it can fairly be construed to be appurtenant to land. *Eastman v Piper, supra*. For examples, see 12 Witkin, Summary of California Law, *Real Property* §384 (10th ed 2005).
- An intended easement will never be construed as personal when it may fairly be construed as appurtenant. *St. Louis v DeBon* (1962) 204 CA2d 464, 22 CR 443.

© The Regents of the University of California

§11.69 b. Transferability

Although easements in gross have been said to be personal and not transferable, they can be transferred if they are expressly referred to in the grant (*Collier v Oelke* (1962) 202 CA2d 843, 846, 21 CR 140) and if they are assignable and inheritable (*Le Deit v Ehlert* (1962) 205 CA2d 154, 166, 22 CR 747). An appurtenant easement may be transferred to a person receiving only a very limited interest in the dominant estate. See *Franceschi v Kuntz* (1967) 253 CA2d 1041, 61 CR 810, in which the court held that the easement holder who had timber and access rights could contract with other persons to do logging and use the access roads.

© The Regents of the University of California

§11.70 8. Ambiguous Description

In general, the land subject to an easement must be described with sufficient certainty to locate it. *PG&E v Crockett Land & Cattle Co*. (1924) 70 CA 283, 233 P 370. However, a right-of-way for road purposes has been upheld even though its location was not fixed in the reservation; the grantee of the right may locate it reasonably, and the grantor may do so if the grantee does not. *Ballard v Titus* (1910) 157 C 673, 683, 110 P 118; *Collier v Oelke* (1962) 202 CA2d 843, 21 CR 140. Acquiescence in a particular use may fix not only the location of the easement but also the nature of its use. *Snodgrass v Crane* (1943) 57 CA2d 565, 134 P2d 862.

The great virtue of a precise description of land location is that it prohibits future variations based on arguments of reasonableness. See *Wilson v Abrams* (1969) 1 CA3d 1030, 82 CR 272, in which the easement holder tried unsuccessfully to have a parking lot agreement construed to permit construction of a service station. See also *Keith v Superior Court* (1972) 26 CA3d 521, 103 CR 314, in which great inconvenience to the servient tenant was held insufficient to permit him to unilaterally relocate a described right-of-way over the dominant tenant's objection. On interpretation of easements, see California Easements and Boundaries: Law and Litigation, chap 1 (Cal CEB 2008).

© The Regents of the University of California

§11.71 9. Uncertain Duration

If an easement is terminated in a manner authorized under CC §811 (see §§11.59-11.64), its extinction may not appear of record. Equally troublesome are ambiguous termination provisions in the document creating the easement.

EXAMPLE: "To *A*, an easement 12 feet wide as long as he needs it for a wagon road." When does *A*'s need terminate? How is his need determined?

Duration should be stated without ambiguity, and if that cannot be done, it is generally better to simply state the purpose, as in §§11.105-11.107.

Railroad rights-of-way create special problems. Railroad rights-of-way created by statute or condemnation are easements, and most privately granted railroad rights-of-way are also construed to be easements (*Great Northern Ry. v U.S*. (1942) 315 US 262, 271, 86 L Ed 836, 845, 62 S Ct 529; *Johnson v Ocean Shore R.R*. (1971) 16 CA3d 429, 433, 94 CR 68). However, the language of each railroad grant is unique and must be considered on a case-by-case basis in determining whether a particular grant is a fee or an easement. *Machado v Southern Pac. Transp. Co*. (1991) 233 CA3d 347, 284 CR 560. On duration of easements, see California Easements and Boundaries: Law and Litigation, chaps 1-2 (Cal CEB 2008).

© The Regents of the University of California

§11.72 10. Failure to Designate as Easement

Another problem with easements arises from the failure to describe them as easements. A grant or reservation of a strip of land, if not expressly qualified as an easement, may result in ownership in fee. *City & County of San Francisco v Union Pac. R.R. Co.* (1996) 50 CA4th 987, 995, 58 CR2d 1. In *Murphy Slough Ass'n v Avila* (1972) 27 CA3d 649, 104 CR 136, a document conveying "a strip of land" along a river was held, in the circumstances, to grant an easement rather than a fee, and the grantor retained his riparian rights.

A conveyance of "all of the mains, pipelines, and all water production, transmission and distribution facilities" was construed to grant an easement even though the word "easement" did not expressly appear. *Maywood Mut. Water Co. No. 2 v City of Maywood* (1972) 23 CA3d 266, 100 CR 174. On interpretation of easements, see California Easements and Boundaries: Law and Litigation, chap 1 (Cal CEB 2008).

© The Regents of the University of California

§11.73 11. Exception or Reservation

In transferring property, a grantor will sometimes wish to withhold an estate, a use less than a fee (*e.g.,* a life estate or an easement), or a portion of the property in fee. The words generally used for these purposes are "excepting" and "reserving." "The difference between the two terms is so slight and shadowy that in common parlance they are used interchangeably." *Van Slyke v Arrowhead Reservoir & Power Co*. (1909) 155 C 675, 680, 102 P 816. Historically, in this country, a reservation amounted to a grant back to the grantor by the grantee. The question of whether a particular provision in a deed is an exception or a reservation is not conclusively determined by the use of the terms alone but depends on the real intention of the parties as ascertained from the whole conveyance. *Main v Legnitto* (1964) 230 CA2d 667, 41 CR 223. To avoid any implication that matters affecting the grantee might impair the grantor's easement rights, the word "exception" seems preferable. For further discussion, see §11.92.

On abolition of the common law rule prohibiting reservation of easements in a stranger, see §11.65. On interpretation of easements, see California Easements and Boundaries: Law and Litigation, chap 1 (Cal CEB 2008).

© The Regents of the University of California

§11.74 12. Failure to State All Purposes and Limitations

Whether the easement is to be exclusive or nonexclusive should be stated expressly in the instrument creating it. If the easement is nonexclusive, it is important to fix responsibility for its maintenance.

Sometimes the statement of purpose is not sufficiently explicit. For example, the phrase "for utility purposes" gives no guidance on whether the utilities are to be underground or aboveground. Similarly, a statement that an easement is "for driveway purposes" does not resolve disputes about whether the driveway may be raised, fenced, or improved with planting. See *Faus v City of Los Angeles* (1967) 67 C2d 350, 62 CR 193, in which the court held that the holder of a municipal electric railway easement could convert from streetcars to buses without forfeiting its easement. On interpretation of easements, see California Easements and Boundaries: Law and Litigation, chap 1 (Cal CEB 2008).

© The Regents of the University of California

§11.75 13. Precautions for Buyers

A purchaser with notice, in the absence of duress or fraud, is deemed to have bargained for the property with the restriction in mind and shown themselves willing to abide by it. *Alfaro v Community Housing Improvement Sys. & Planning Ass'n* (2009) 171 CA4th 1356, 1385, 89 CR3d 659 (restriction on resale price). To protect against claims of easements or other title defects clouding the title of the land, buyers can and should do several things:

- The purchase agreement should provide that the seller represents and warrants that no such clouds exist, or at least that seller has no knowledge of any such clouds.
- The buyer can inspect the property, which will also buttress a defense of bona fide purchaser without notice if a claim later arises.
- A preliminary report should be requested in a timely manner, and copies of the documents referred to as exceptions should be requested from the title company and read. On preliminary reports generally, see California Title Insurance Practice, chap 5 (2d ed Cal CEB 1997).
- The buyer should consider a survey. On surveys, see Title Ins §§4.30-4.34.
- The buyer should request an American Land Title Association (ALTA) owner's policy of title insurance with survey endorsement, if the expense seems warranted. The usual form of protection is title insurance in the proper amount (although title insurance does not eliminate valid claims that may exist). Again, buyers should be advised about the different forms of coverage and informed that standard-coverage policies often insure only matters of record; matters that would be revealed only by inspection of the land are covered only under the more expensive ALTA form of owner's policy. *Contini v Western Title Ins. Co.* (1974) 40 CA3d 536, 543, 115 CR 257. On ALTA policies, see Title Ins, chaps 6-8, Apps F-H.

The purchase agreement can be drafted to provide that, if a cloud on the title is discovered that the title insurer cannot insure against, the buyer has the choice of demanding correction or waiving the defect and acquiring the property with an appropriate deduction, to be held in escrow or credited to the purchase price.

NOTE: A buyer's current willingness to accept a cloud on title may still result in an impairment when that buyer, in turn, attempts to sell or encumber the property.

Exceptions to title policies can often be negotiated, and title insurers will occasionally accept indemnities or otherwise assume the risk of insurance as part of their underwriting process. It is also possible that title insurers will eliminate exceptions under a lender's policy, but retain the exception as to the owner's coverage if the title defect is minor and unlikely to impair the lender's security. See *Lawrence v Chicago Title Ins. Co*. (1987) 192 CA3d 70, 75, 237 CR 264. On title insurance and easements, see California Easements and Boundaries: Law and Litigation, chap 9 (Cal CEB 2008).

© The Regents of the University of California

§11.76 14. Precautions for Sellers

If the seller elects to make warranties or representations of title as part of the transaction, the seller's lawyer must underscore the difference between warranties and statements that are made only of the seller's knowledge. The safest course for the seller is to convince the buyer to rely on the buyer's inspection of a preliminary report and receipt of the appropriate title policy through escrow at closing.

If a seller makes a representation of title based on its own knowledge, care should be taken as to the state of knowledge of the seller's employees or as to matters that may be in the seller's files. If warranties are issued, care should be taken to structure them to be consistent with the seller's existing title insurance.

Sellers of residential property should be aware that the required forms of disclosure statements provide for encroachments, easements, and similar matters affecting the property. CC §1102.6. When the seller knows of facts materially affecting the value or desirability of the property, which are known or accessible only to the seller, and when the seller also knows that such facts are not known to, or within the reach of, the diligent attention and observation of the buyer, the seller has a duty to disclose those facts to the buyer. *Lingsch v Savage* (1963) 213 CA2d 729, 735, 29 CR 201.

See §4.120 for discussion of "as is" sales.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/11 Descriptions of Property/§11.77 15. Adverse Possession, Prescription, and Implied Dedication

§11.77 15. Adverse Possession, Prescription, and Implied Dedication

Adverse possession, prescription, and implied dedication may affect all or part of the record owner's title. Prescription refers to the creation of easements by adverse use over a period of time. See California Easements and Boundaries: Law and Litigation, chap 1 (Cal CEB 2008); Benz & Merritt, *Fences, Boundaries, and Prescriptive Easements,* 23 CEB Real Prop L Rep 122 (Apr. 2000). Adverse possession refers to the acquisition and extinguishment of possessory interests. Implied dedication refers to the owner's intent to dedicate property to public use.

The elements of adverse possession and prescription are set forth in CC §1007 and CCP §§321-325. See also *Gilardi v Hallam* (1981) 30 C3d 317, 321, 178 CR 624; *Mehdizadeh v Mincer* (1996) 46 CA4th 1296, 54 CR2d 284. The elements of establishing title by adverse possession are tax payment and open and notorious use or possession that is continuous and uninterrupted, hostile to the true owner, and under a claim of title. To constitute adverse possession by someone claiming under color of title, land is deemed to have been possessed when it has been cultivated or improved, protected by a substantial enclosure or, if not enclosed, when it has been used to supply fuel or timber, for husbandry or pasturage, or for the occupant's ordinary use. CCP §323. When a known farm or single lot has been partly improved, the unimproved portion is deemed occupied for the same length of time. CCP §323(4). When color of title is not present, land is deemed to have been possessed when it is protected by a substantial enclosure or is cultivated or improved. CCP §325.

NOTE: Land dedicated to public entities and public utilities is not subject to title by prescription. CC §1007. Under *Hays v Vanek* (1989) 217 CA3d 271, 266 CR 856, land dedicated to quasi-public use, even if not accepted for such dedication, is not subject to adverse possession.

Acquisition of title by adverse possession between tenants in common requires, in addition to exclusive possession, open, notorious, and unequivocal evidence of intent to oust the nonoccupying tenant of its interest in the common property. *Preciado v Wilde* (2006) 139 CA4th 321, 325, 42 CR3d 792.

There is no policy favoring prescriptive easements; a claimant has the burden of proof by clear and convincing evidence. *Grant v Ratliff* (2008) 164 CA4th 1304, 1310, 79 CR3d 902; *Brewer v Murphy* (2008) 161 CA4th 928, 938, 74 CR3d 436.

A claimant who cannot claim adverse possession for failure to pay taxes on the disputed property may not obtain a prescriptive easement that extends so far that it becomes the equivalent of a fee interest and dispossesses the record title owners of part of their property. *Kapner v Meadowlark Ranch Ass'n* (2004) 116 CA4th 1182, 1186, 11 CR3d 138; *Harrison v Welch* (2004) 116 CA4th 1084, 1092, 11 CR3d 92; *Mehdizadeh v Mincer* (1996) 46 CA4th 1296, 1303, 54 CR2d 284.

In *Gion v City of Santa Cruz* (1970) 2 C3d 29, 84 CR 162, the California Supreme Court held that to negate a finding of implied intent to dedicate a right-of-way to the public, based on uninterrupted public use for more than 5 years, an owner must affirmatively show that he or she either granted the public a license or made a bona fide attempt to prevent public use. In response to *Gion,* the legislature in 1971 amended CC §813 and added CC §1009, which state that, except for land within 1000 yards of the ocean and harbors, estuaries, bays, and inlets, no such implied intent to dedicate would be found, and no public use would ripen into an easement, without that owner's written irrevocable offer to dedicate. The legislation has been held to be effective from March 4, 1972, the date of its enactment. *Friends of the Trail v Blasius* (2000) 78 CA4th 810, 93 CR2d 193. See also *County of Los Angeles v Berk* (1980) 26 C3d 201, 161 CR 742; *Bess v County of Humboldt* (1992) 3 CA4th 1544, 1550, 5 CR2d 399; *City of Long Beach v Daugherty* (1977) 75 CA3d 972, 142 CR 593; *County of Orange v Chandler-Sherman Corp.* (1976) 54 CA3d 561, 126 CR 765; *Richmond Ramblers Motorcycle Club v Western Title Guar. Co*. (1975) 47 CA3d 747, 121 CR 308.

NOTE: The scope of pre-March 1972 public recreational uses of private property that give rise to an implied dedication defines the scope of contemporary uses. *Burch v Gombos* (2000) 82 CA4th 352, 98 CR2d 119. See Comment in 23 CEB Real Prop L Rep 280 (Oct. 2000).

For many years in California an implied dedication to the public was possible under the former Act of July 26, 1866 (43 USC §932 (repealed effective Oct. 21, 1976)) and former California Political Code §§2618-2622 (in effect from 1872 to 1935). Such dedication could occur through establishment of a route as a highway by a public authority or by use by the public deemed sufficient in law to constitute an acceptance of the implied offer of dedication. *Union Transp. Co. v Sacramento County* (1954) 42 C2d 235, 244, 267 P2d 10; *City of Venice v Short Line Beach Land Co.* (1919) 180 C 447; *Hanshaw v Long Valley Road Ass'n* (2004) 116 CA4th 471, 477, 11 CR3d 357; *Western Aggregates, Inc. v County of Yuba* (2002) 101 CA4th 278, 292, 130 CR2d 436; *Ball v Stephens* (1945) 68 CA2d 843, 845, 158 P2d 207. These provisions are relevant to roads created in the 1930s and before. Use of express private easements by adjacent property owners and their invitees is not sufficient evidence for an implied dedication. *Biagini v Beckham* (2008) 163 CA4th 1000, 1013, 78 CR3d 171. On implied dedications, see Easements, chaps 1, 9.

Posting signs in the manner prescribed in CC §1008 prevents a use from ripening into a prescriptive easement. If an owner's efforts to exclude the public or discourage public use have effectively put the public on notice that its use of the property is unauthorized, the owner can defeat the accrual of a public easement. In *County of Los Angeles v Berk* (1980) 26 C3d 201, 216, 161 CR 742, the court held that defendants and the former property owners had not fulfilled the burden of putting the public on notice.

EXAMPLE: An implied dedication was found in *Brumbaugh v County of Imperial* (1982) 134 CA3d 556, 562, 184 CR 11, in which the court differentiated between dedication implied in fact ("by the affirmative acts or acquiescence of the property owner") and dedication implied in law ("by the continuous adverse public use of the property throughout the prescriptive period without substantial interference by the owner").

© The Regents of the University of California

C. Doctrines of Agreed Boundaries and of Practical Location

§11.78 1. Doctrine of Agreed Boundaries

When the true boundary line between properties of coterminous owners is uncertain, a new boundary line will become for all purposes the boundary between the properties if the owners enter into an express or implied agreement fixing the boundary line and accept and acquiesce in the line either (1) for a period equal to the statute of limitations or (2) under such circumstances that substantial loss would be caused by a change of position. *Bryant v Blevins* (1994) 9 C4th 47, 36 CR2d 86. See also *French v Brinkman* (1963) 60 C2d 547, 551, 35 CR 289; *Ernie v Trinity Lutheran Church* (1959) 51 C2d 702, 707, 336 P2d 525. Agreed boundary lines were traditionally favored because early surveys in the state could be most uncertain, and in later years the monuments and landmarks they described could often not be found. *Kraemer v Superior Oil Co*. (1966) 240 CA2d 642, 650, 49 CR 869. Legal uncertainty about an original map need be shown only by circumstantial evidence. *Vella v Ratto* (1971) 17 CA3d 737, 741, 95 CR 72. Long-standing walls, fences, or similar monuments have been recognized as evidence of agreement by earlier owners. *Kunza v Gaskell* (1979) 91 CA3d 201, 154 CR 101; *Vella v Ratto, supra.*

However, the mere presence of a fence is not sufficient; the doctrine still requires (1) uncertainty about the location of the true boundary when the fence was erected and (2) an agreement between the neighboring property owners to use the fence's location as the means of establishing the boundary. In addition, courts recognize that barriers are built for many reasons, only one of which is to act as a visible barrier between parcels. *Bryant v Blevins* (1994) 9 C4th 47, 36 CR2d 86.

The doctrine is particularly powerful because it does not depend on record title, and the authorities concur that the agreed-on line becomes in effect the true line and attaches itself to the deeds. *Ernie v Trinity Lutheran Church* (1959) 51 C2d 702, 708, 336 P2d 525; *Young v Blakeman* (1908) 153 C 477, 482, 95 P 888. The issue of payment of taxes is also immaterial to the doctrine. *Ernie,* 51 C2d at 709. It is presumed that taxes were assessed by the assessor and that value was placed on the land and improvements of each party as disclosed by visible possession, rather than as would be disclosed by a survey. *Price v DeReyes* (1911) 161 C 484, 489, 119 P 893; *Caballero v Balamotis* (1956) 144 CA2d 58, 61, 300 P2d 363; *Carr v Schomberg* (1951) 104 CA2d 850, 860, 232 P2d 597.

Case law has not been consistent on how to establish, for purposes of this doctrine, the required uncertainty as to the true boundary. Several recent cases have rejected application of the doctrine of agreed boundaries when surveyors' monuments and reliable legal descriptions are present, events are recent, and witnesses are still living. *Armitage v Decker* (1990) 218 CA3d 887, 903, 267 CR 399; *Mesnick v Caton* (1986) 183 CA3d 1248, 1257, 228 CR 779. *Armitage* indicates that this doctrine will not be applied, and the boundary will not be considered uncertain, if it can be made certain by a survey.

The doctrine does not apply when there is no evidence that a fence was built to resolve a disagreement between the owners about the true boundary line. *Bryant v Blevins*, *supra; Mehdizadeh v Mincer* (1996) 46 CA4th 1296, 54 CR2d 284.

On doctrine of agreed boundaries, see California Easements and Boundaries: Law and Litigation, chaps 8, 10 (Cal CEB 2008).

© The Regents of the University of California

§11.79 2. Doctrine of Practical Location

A close corollary to the doctrine of agreed boundaries is the doctrine of practical location. Under this doctrine, if an owner conveys a parcel of a large tract that is delineated on the ground by fixed monuments, these monuments will prevail over any differing description in the deed if the parties rely on them as established in the intended boundaries—even if the monuments differ from those that a survey would reveal. *French v Brinkman* (1963) 60 C2d 547, 551, 35 CR 289.

© The Regents of the University of California

§11.80 D. Abandonment and Vacation

Except for titles held in fee, lawyers should not assume that interests appearing of record or revealed by inspection are as they appear to be. They may have been abandoned or vacated. Abandonment of a right in land requires that the owner of the right

- intended to abandon it; and
- gave evidence of this intent by acts or failures to act that are clear, unequivocal, and decisive.

See 12 Witkin, Summary of California Law, *Real Property* §§422-424 (10th ed 2005).

The doctrine of abandonment does not apply to a fee simple interest in real property. However, certain fee interests such as perpetual easements and perpetual profits derived from land, including oil and gas interests, can be abandoned. *Gerhard v Stephens* (1968) 68 C2d 864, 69 CR 612.

If an interest has been abandoned, the description of the property may be affected. Thus, if an appurtenant easement has been abandoned, its description as part of the transfer will not pass the right to the buyer (except to the extent the rights of a bona fide purchaser apply as discussed in §§15.85-15.87). Generally, the abandonment should be established by agreement, deed, or judgment.

On vacation of street easements and the closing of streets and highways to public use, see Str & H C §§8300-8363. On abandonment, see California Easements and Boundaries: Law and Litigation, chaps 1, 9 (Cal CEB 2008).

© The Regents of the University of California

§11.81 E. Effect of Water on Land

Physical changes resulting from the action of water on real property raise many questions. Other problems arise from the imprecise use of water monuments as points or boundaries in descriptions. Some of these problems may be eliminated by careful drafting (see §11.103), but others may arise even after the most careful drafting. Such problems most commonly arise regarding the following issues:

- High-water mark, low-water mark (see §11.82);
- Thread or middle of lake or stream (see §11.83);
- Islands (see §11.84);
- Formerly navigable waters (see §11.85); and
- Avulsion (see §11.86).

On easements relating to water, see California Easements and Boundaries: Law and Litigation, chap 3 (Cal CEB 2008).

© The Regents of the University of California

§11.82 1. High-Water Mark, Low-Water Mark

In the absence of contrary evidence of intent in the grant, land bordering tidewaters extends to the high-water mark. On inland waters (including Monterey Bay), see *U.S. v California* (1965) 381 US 139, 14 L Ed 2d 296, 85 S Ct 1401. Land on a navigable lake or stream extends to the low-water mark. CC §830; CCP §2077. These marks may shift as the water deposits sand or soil (alluvion), thus augmenting the land on the bank (accretion), or as it recedes (reliction) or encroaches on the land. If the change is gradual and of natural causes, the owner's land is augmented or diminished by the shifting of the water boundary. CC §1014; *Raglan v Johnston Rock Co*. (1942) 50 CA2d 705, 123 P2d 883. The shifting of tides, however, makes ascertaining high-water marks extremely difficult. See discussion in *People v William Kent Estate Co*. (1966) 242 CA2d 156, 51 CR 215, and its use of the expression "neap" tides. See also *Lechusa Villas W. v California Coastal Comm'n* (1997) 60 CA4th 218, 235, 70 CR2d 399, for an elaboration on the boundary line standard articulated in *People v William Kent Estate Co., supra.* The State owns all tidelands below the ordinary high water mark, and holds such lands in trust for the public. CC §670; *State of Cal. ex rel State Lands Comm'n v Superior Court* (1995) 11 C4th 50, 63, 44 CR2d 399; *Burke v California Coastal Comm'n* (2008) 168 CA4th 1098, 1103, 85 CR3d 909 (ambulatory boundary settlement). For discussion of the history of California sea boundary disputes and engineering methods for determining those boundaries, see Shalowitz, Shore and Sea Boundaries (1962, 1964). A complete procedure for establishing boundaries on tidal and submerged lands by agreement and by quiet title is set forth in Pub Res C §§6357-6360.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/11 Descriptions of Property/§11.83 2. Thread or Middle of Lake or Stream

§11.83 2. Thread or Middle of Lake or Stream

The owner of land bordering on a nonnavigable lake or stream is presumed to take to the thread or middle of the lake or stream (CC §830; CCP §2077) unless otherwise stated in the instrument. Accretion, reliction, erosion, or encroachment may change the location of the thread.

© The Regents of the University of California

§11.84 3. Islands

Islands may be formed by accretion, by the recession of the water, or by a new watercourse isolating land that was formerly part of the mainland. Islands in navigable streams belong to the state if there is no title to the contrary (CC §1016), even if the water between the island and the bank is not navigable. *Packer v Bird* (1886) 71 C 134, 11 P 873. An island in a nonnavigable stream belongs to the owner of the shore. If the island lies entirely on one side of the thread, it belongs to the owner of the shore on that side; if it bestrides the thread, the owners on the opposite banks own it up to the midstream dividing line. CC §1017. If a new channel forms an island by separating a portion of the land from the property to which it was attached, it continues to belong to the owner of that land. CC §1018.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/11 Descriptions of Property/§11.85 4. Formerly Navigable Waters

§11.85 4. Formerly Navigable Waters

If waters cease to be navigable, two important rights arise:

- The state may sell to abutting owners the underlying land thus made available or may exchange an abandoned navigable river or slough for lands having equal or greater value (Pub Res C §6210.8); and
- Persons claiming an interest in property lying in the former bed may bring quiet title actions against the state to determine ownership (Pub Res C §6461).

© The Regents of the University of California

§11.86 5. Avulsion

As distinguished from the gradual processes of accretion, reliction, or erosion, avulsion is the sudden removal of land from the estate of one owner of the shore or bank to that of another as a result of the action of the water. The owner of a distinguishable part of a bank that is suddenly carried away and deposited elsewhere may reclaim it within 1 year. CC §1015; 12 Witkin, Summary of California Law, *Real Property* §237 (10th ed 2005).

Avulsion can also be caused by the deposit of artificial fill. In this case, the newly created property belongs to the owner of the submerged land on which the fill is deposited—not the owner of the dry land adjacent to the fill. See *New Jersey v New York* (1998) 523 US 767, 140 L Ed 2d 993, 1013, 118 S Ct 1726.

© The Regents of the University of California

§11.87 F. Eminent Domain

Actions by the state or an authority with the power of eminent domain to acquire portions of real property, typically for acquisition of rights-of-way for streets and highways, can affect land descriptions and should be ascertainable by inspections of record title and the land. CCP §§1240.010-1273.050. See also CC §1009(d) (regarding implied dedication) and §1001 (relating to acquisition of private easements for necessary utilities through a private power of eminent domain). For a thorough discussion of the eminent domain power, see Condemnation Practice in California (3d ed Cal CEB 2005).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/11 Descriptions of Property/§11.87A G. Merger of Parcels

§11.87A G. Merger of Parcels

Contiguous parcels under common ownership are subject to merger under the Subdivision Map Act (Govt C §§66410-66499.37) if (1) any one of the parcels does not conform to the standards for minimum parcel size of the local zoning ordinance (Govt C §66451.11); and (2) at least one parcel is undeveloped by any structure for which a building permit was issued or for which a building permit was not required at the time of construction, or is developed only with an accessory structure or structures or with a structure other than an accessory structure that is partially sited on a contiguous parcel (Govt C §66451.11(a)). In addition, each parcel to be merged must meet at least one of the following conditions (Govt C §66451.11(b)):

- It is less than 5000 square feet;
- It was not created in compliance with applicable laws and ordinances;
- It does not meet current standards for sewage disposal or domestic water supply;
- It does not meet current standards for slope stability;
- It lacks adequate legal access for vehicles or safety equipment;
- Its development would create health or safety hazards; or
- It is inconsistent with the applicable general plan. Govt C §§66451.11, 66451.30.

The process requires a local ordinance that conforms to and implements the Government Code provisions, notice and a public hearing, and filing of notice of merger of record. Govt C §§66451.10-66451.32.

© The Regents of the University of California

§11.88 H. Estoppel

A boundary may be changed by estoppel. *Helm v Wilson* (1888) 76 C 476, 18 P 604. Estoppel occurs when adjoining owners recognize a dividing line and one owner then makes such valuable improvements on the basis of the line that it would be inequitable to require that owner to remove or abandon them if the other owner later disagrees on the location of the boundary.

© The Regents of the University of California

V. ELIMINATING DEFECTS IN DESCRIPTIONS

A. Solutions to Typical Problems

§11.89 1. Overlapping Descriptions

If a seller owns a rectangular lot that is less than 100 feet wide but conveys "to *B* the easterly 50 feet measured perpendicularly to the easterly boundary" and "to *C* the westerly 50 feet measured perpendicularly to the westerly boundary," an overlapping description is created, because the total width conveyed is 100 feet although the lot is not that wide.

If the deed to *B* is the first recorded, *C* must take a grant with constructive notice that the easterly 50 feet have already been conveyed to *B*. In addition, the seller can convey no greater title to *C* than the seller already possesses. Nevertheless, *B*'s title may be clouded by the conveyance to *C*, even though the deed to *C* would be out of *B*'s chain of title. If *C* makes any claim on the record title of *B*, then *B* would generally be entitled to defense under a title insurance policy.

To eliminate the cloud on *B*'s title, *B* and *C* could execute and record a boundary line agreement or *C* could quitclaim the legal description conveyed to *B*. As a last resort, a quiet title action could be brought to obtain a recordable decree quieting title.

© The Regents of the University of California

§11.90 2. Failure to Close Metes and Bounds Description

The requirements of a metes and bounds description are set forth in §§11.26-11.39. One requirement is that it close, *i.e.,* that no gap be left in the boundaries. If a description of record is found to leave a gap, an engineer or a surveyor should be retained to draft a proper description unless the missing element is obvious from the face of the document. Often, the grantor in whose instrument the gap first appeared can be found and induced to execute a new deed. If there are intervening owners, the deed from the first grantor should, if possible, conform to the requirements of after-acquired title (see §12.10).

The rules construing descriptions of CCP §2077 or the doctrines of agreed boundary line, practical location, or adverse possession may often resolve a defective legal description. See §§11.77-11.79.

The two judicial solutions are quiet title or reformation. In this context, declaratory relief is treated as a variant of quiet title. On quiet title actions, see California Real Property Remedies and Damages, chap 7 (2d ed Cal CEB 2002); 8 Grossman & Van Alstyne, Pleading—Civil Actions §§1053-1056 (2d ed 1981); 5 Witkin, California Procedure, *Pleading* §§613-629 (5th ed 2008).

On reformation, see Real Property Remedies, chap 2; 5 Witkin, California Procedure*, Pleading* §§762-774.

© The Regents of the University of California

§11.91 3. Incomplete, Confusing, or Erroneous Descriptions

A description may be incomplete in itself (*e.g.,* it fails to state county or tract number) or become incomplete as a result of an event (*e.g.,* a monument has disappeared). Similarly, although a description may seem to be complete, it may be contradictory, *e.g.,* an incorrect legal description followed by correct street address.

As long as the instrument is properly recorded and indexed, the description may still impart constructive notice. *Rogers v McCartney* (1906) 3 CA 34, 35, 84 P 215. If it is possible from the whole description to ascertain and identify the land intended to be conveyed, it will not be void and will retain its priority. *Leonard v Osburn* (1915) 169 C 157, 161, 146 P 530; *Bond v Aickley* (1914) 168 C 161, 164, 141 P 1188 (deed sufficient even though word "feet" omitted); *Crouse-Prouty v Rogers* (1917) 33 CA 246, 248, 164 P 901 (deed valid despite misdescription on tract map); *Black Eagle Oil Co. v Belcher* (1913) 22 CA 258, 261, 133 P 1153 (deed valid despite misdescription of base and meridian).

In some instances, the lawyer must first obtain a valid description from a competent engineer or surveyor and then seek relief by agreement with the property owner's predecessors in interest. If relief cannot be agreed on for any reason, the solution lies in an action for reformation or quiet title. See §11.90 for references to works on quiet title and reformation actions.

© The Regents of the University of California

§11.92 4. Reservation or Exception in Successive Descriptions

If *B* is the grantee under a deed that excepted (or reserved) an estate less than a fee or a described strip of land or subsurface mineral rights, use of the same exception in the next conveyance may create ambiguities about the ownership of the excepted interest.

EXAMPLE: *A* grants to *B*, reserving an easement in favor of *A*'s adjacent land; *B* grants to *C*, "reserving" the same easement. Has *B* clouded *A*'s title to the easement by ostensibly reserving it for himself? Or has *B* attempted to indicate that he, too, expects to use the easement for the benefit of another parcel of adjacent property, rather than merely excluding *A*'s reserved interest? To eliminate this ambiguity, *B*'s deed should state clearly the property for the benefit of which he makes the exception if it is a parcel other than *A*'s, or should make the deed "subject to the easement reserved in deed from *A* to *B* recorded at…."

© The Regents of the University of California

§11.93 5. Fraudulent or Erroneous Surveys

In the early days of California, some surveys made under government contract misplaced such markers as rivers, mountains, and section corners. For instance, in *Schwartz v Dibblee* (1921) 51 CA 451, 197 P 125, the question turned on the fact that the surveyor of section 30 had discovered that the south line of adjacent section 19 was ten chains too far north.

Even when official surveys are erroneous, they benefit from the presumption that official duties were properly performed. *Southern Pac. Land Co. v Meserve* (1921) 186 C 157, 198 P 1055. However, public lands may be resurveyed if the resurvey would not impair the bona fide rights or claims of any owner or claimant. 43 USC §772; Bureau of Land Management, Manual of Instructions for the Survey of the Public Lands of the United States §§387, 409, 428 (1973). For information on the next edition of this manual, see Directory. See also Official Maps in Govt C §§66499.50-66499.58.

In a private, unofficial survey, the presumption that an official duty has been properly performed does not apply; a correct survey is admissible to show the error of a prior survey. The remedy is then by agreement, reformation, or quiet title.

© The Regents of the University of California

B. Drafting to Eliminate Defects

§11.94 1. Drafting Principles

The following principles of good drafting apply to descriptions generally:

- Avoid nonessential language (see §11.95);
- Avoid ambiguity (see §11.96);
- Use precise language (see §11.97); and
- Know the statutory rules of construction (see §11.98).

© The Regents of the University of California

§11.95 a. Avoid Nonessential Language

Language that is not essential to the description should be avoided.

EXAMPLE: If the southwest quarter is assumed to consist of 160 acres but the exact area is not a substantial factor in the transaction, the addition of the information "consisting of 160 acres" opens possibilities for conflict and litigation.

For a comparison of merits and hazards in adding acreage to descriptions, see §11.16.

© The Regents of the University of California

§11.96 b. Avoid Ambiguity

Occasionally, poor descriptions are supplemented in later deeds with an additional description that redescribes the area believed to be encompassed by the earlier language. Unfortunately, this supplementation adds ambiguity to the instrument. The correct remedy is a survey, agreement with contiguous owners, a quiet title decree, or another appropriate solution. If more than one description is helpful, specify which is to control. If the two prove to be inconsistent, the rules of CCP §2077 on interpreting property descriptions may control.

© The Regents of the University of California

§11.97 c. Use Precise Language

Appurtenances (*i.e.,* augmenting easements, additional rights, personal property, and similar elements transferred in addition to the principal property) should be described with the same care as the property itself. Easements, for example, being interests in real property, bring into play all the principles discussed in this chapter. Easements are more fully discussed in §§11.43-11.77, and forms are presented in §§11.105-11.107. When personal property is being transferred with real property, it should be identified with particularity in the agreement and in a bill of sale separate from the deed. A vague description, such as "all the living room furniture," may lead to later disputes and even to attempted circumvention of the parties' intent. Generally, an agreed and initialed inventory, describing the goods precisely, is the most satisfactory method. On occasion, equipment may be photographed and the photographs made part of the agreement.

© The Regents of the University of California

§11.98 d. Know Statutory Rules of Construction

As noted in §§11.14-11.15, parol evidence can be introduced to interpret deeds. Code of Civil Procedure §2077 supplies a number of rules of construction that control if other, sufficient information is unavailable, including the following rules:

- Definite and ascertained particulars in the description control over information that is indefinite, unknown, or false;
- Permanent and visible or ascertained boundaries or monuments control over inconsistent lines, angles, or surfaces;
- Between different measurements that are inconsistent, lines control over angles, and angles control over surfaces;
- The grantor's rights are usually construed to the middle of roads and nonnavigable streams, to high-water marks of tidewater, or to low-water marks of navigable waters that have no tide; and
- When a description refers to a map, the map controls if it appears that the parties act with reference to the map; otherwise, the map is subordinate to any definite and ascertained particulars.

© The Regents of the University of California

§11.99 2. Drafting Particular Descriptions

Many principles discussed under reading descriptions (see §§11.14-11.41) apply equally to drafting descriptions. For instance, the drafter must know about off-record matters (see §§11.53-11.57, 11.77-11.79) so that they may be either confirmed (by including necessary provisions in the agreement or deed) or removed (by clearing the record before the transaction is consummated).

Forms for the kinds of descriptions most commonly encountered in California are set out in §§11.100-11.102. The elements in the forms apply whether the description is part of a deposit receipt, escrow instructions forming a bilateral contract, or a more formal purchase and sale agreement. See *Beverage v Canton Placer Mining Co*. (1955) 43 C2d 769, 278 P2d 694; *Alameda Belt Line v City of Alameda* (2003) 113 CA4th 15, 21, 5 CR3d 879. The drafting principles discussed in §§11.94-11.98 apply in drafting the particular descriptions that follow.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/11 Descriptions of Property/§11.100 3. Form: Description by Reference to Subdivision Map

§11.100 3. Form: Description by Reference to Subdivision Map

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§11.100-11.102.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

11.100-1 Description by reference to subdivision map

The real property in the _ _[*City of* _ _[*name*]_ _*,/City and*]_ _ County of _ _[*name*]_ _, State of California, described as _ _[*lot, block, tract, or other designation used on map*]_ _ per map recorded in book _ _, page(s) _ _, of Maps, Office of County Recorder of _ _[*name*]_ _ County.

Comment: This provision describes property by referring to a recorded subdivision map. The recorder may record in a book of subdivision maps, a book of parcel maps, or a book of cities and towns. Govt C §66466.

Statutory authority for description by reference to a subdivision map is given in §11.24, which also cites code sections that permit the recording of maps and warns of consequences flowing from improperly recorded maps.

For marketing purposes, subdivisions sometimes bear names (*e.g.,* Northbrae, Hiawatha Park) instead of or in addition to numbers. If the name is shown on the recorded map, it is a proper part of the description. If it is the only designation of the subdivision (*i.e.,* there is no tract number), the name becomes a necessary part of the description.

On descriptions for transfers of fewer than all the parcels shown on the map, see forms and Comments in §§11.101-11.102.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/11 Descriptions of Property/§11.101 4. Form: Description by Reference to Rectangular Survey Map

§11.101 4. Form: Description by Reference to Rectangular Survey Map

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§11.100-11.102.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

11.101-1 Description by reference to rectangular survey map

The real property in the _ _[*City of* _ _[*name*]_ _*,/City and*]_ _ **County of** _ _[*name*]_ _**, State of California, described as** _ _[*e.g., SW quarter*]_ _**, section** _ _**, township** _ _**, range** _ _**,** _ _[*Humboldt/Mt. Diablo/San Bernardino*]_ _ **base and meridian,** _ _[*per survey of* _ _[*date*]_ _]_ _**.**

Comment: This provision describes property by reference to a United States government rectangular survey, discussed in §§11.17-11.21. If there has been more than one survey or plat (see §11.93), the date of the one referred to must be given; if it is not known whether there was more than one, inserting the date is a simple precaution.

If an oddly shaped parcel is being transferred (*e.g.,* Lot 1, section 1, as shown in Figure 1, §11.18), or if the property cannot be described as a quarter or a half, the form should be modified to read:

described as _ _[*that/those*]_ _ **portion(s) of** _ _[*specify, e.g., quarters or section*]_ _ _ _[*state other qualifications*]_ _**:** _ _[*Describe*]_ _**.**

An example of a description of an oddly shaped parcel:

described as that portion of section 30, township 2 north, range 4 east, San Bernardino base and meridian lying southerly of the lands described in deed from R. Quinn to B. Quinn recorded in book….

If, instead, a transfer is to be described in terms of lands excluded, the following should be added:

EXCEPT _ _[*that/those*]_ _ **portion(s)** _ _[*specify parts not included in transfer*]_ _**.**

"Except" has a precise legal meaning and is defined in §11.73. It is capitalized in this form because it is customary to do so in descriptions. For additional elements in descriptions, see §§11.94-11.98.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/11 Descriptions of Property/§11.102 5. Form: Description by Reference to Deed or Other Instrument

§11.102 5. Form: Description by Reference to Deed or Other Instrument

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§11.100-11.102.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

11.102-1 Description by reference to deed or other instrument

The real property in the _ _[*City of* _ _[*name*]_ _*,/City and*]_ _ **County of** _ _[*name*]_ _**, State of California, described as** _ _[*that/those*]_ _ **portion(s) of the property described in** _ _[*specify document, e.g., deed, judgment, or other*]_ _ **of** _ _[*date*]_ _**, in which** _ _[*name(s)*]_ _ _ _[*is/are*]_ _ _ _[*specify designation in document, e.g., grantor, plaintiff, or other designation*]_ _ **and** _ _[*name(s)*]_ _ _ _[*is/are*]_ _ _ _[*specify designation, e.g., grantee, defendant, or other designation*]_ _**, recorded on** _ _[*date*]_ _**, as Instrument** _ _ _ **in book** _ _ _**, page** _ _ _ **of** _ _[*official book*]_ _**, of the Office of the County Recorder of** _ _[*name*]_ _ **County.**

Comment: Land may be described by reference to another instrument. See §11.25. However, the description will be improper if (1) the description in the previously recorded instrument is faulty or (2) the reference to that instrument in the present document is faulty. To protect against both pitfalls, the attorney should examine the map or other instrument or obtain adequate assurance from the title company, and carefully compare that information with the reference in the new instrument. Copies of maps can usually be obtained from title companies, assessors' offices, city or county engineers, or zoning offices, although title company maps are generally preferable.

Descriptions by reference to an instrument that is not of public record should be avoided. The validity of the new conveyance does not depend on whether the instrument referred to is of record (*Saunders v Schmaelzle* (1874) 49 C 59, 66), but serious problems of proof and constructive notice may arise if it is not.

The document to which reference is made should be described by date, parties, designation of the parties in the document, and any recording data. For other elements in descriptions, see §§11.94-11.98. If any part of the property described in the other document is to be excluded from the present transfer, the exclusion or exception should be clearly shown. See §11.73.

© The Regents of the University of California

§11.103 6. Description by Metes and Bounds

Descriptions by metes and bounds are so diverse that they do not lend themselves to a single form. In general, the rules for reading these descriptions (see §§11.26-11.39) are also the rules for drafting them. For rules of construction, see CCP §2077. As experience in drafting descriptions is acquired, other rules will become apparent.

EXAMPLE: Parallel lines in a single description use the same numbers but opposite directions (*e.g.,* S 79° 12' 10" E is parallel to N 79° 12' 10" W).

If the metes and bounds consist of bearings, angles, arcs, and distances, the drafter should use only those measurements that have been certified by a qualified surveyor or engineer. These experts may not be necessary for metes and bounds descriptions based entirely on physical monuments, but, because of difficulty in identifying both natural and artificial physical monuments, a description by surveyors' courses is generally preferable.

Only the most recent survey should be used. All surveys should be read critically to make certain that the area is closed and should be compared with other pertinent data (including record title to prevent record gaps or overlaps). If inconsistencies with prior deeds in the chain of title appear, the remedies discussed in §11.90 may become necessary to avoid a cloud on the title. For an example of discrepancies to be avoided, see *Schwartz v Dibblee* (1921) 51 CA 451, 197 P 125. If water, streets, or mountains are boundaries, it is wise not to rely on the rules of construction in CC §§830-831, 1112, CCP §2077(4), or Govt C §§23073-23076. It is best to specify thread of river, center of road, middle of lake, ridge of mountain, and so forth, if that is what is meant. On waters, see §§11.81-11.86. For additional drafting principles, see §§11.94-11.98. On railroad easements, see *Faus v Nelson* (1966) 241 CA2d 320, 50 CR 483.

Successive numbering of the calls (see Example 2 in §11.38) contributes to easy reading and to the drafter's accuracy.

© The Regents of the University of California

§11.104 C. Easements

Easement problems are discussed in §§11.43-11.77, and precautions for buyers and sellers are listed in §§11.75-11.76. Many of the problems discussed in those sections can be eliminated by proper drafting. Forms for that purpose are set out in §§11.105-11.107.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/11 Descriptions of Property/§11.105 1. Form: Reservation of Easement in Grantor

§11.105 1. Form: Reservation of Easement in Grantor

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§11.105-11.107.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

11.105-1 Reservation of easement in grantor

_ _[*Describe parcel conveyed*]_ _ **excepting from that property** _ _[*describe property covered by easement*]_ _ **as an easement** _ _[*personal and in gross to grantor/appurtenant to* _ _[*describe dominant tenement*]_ _]_ _ _ _[*describe purpose, e.g., providing ingress to and egress from the dominant tenement*]_ _ **for** _ _[*specify duration, e.g., such time as the dominant tenement shall abut on a public road or street*]_ _**.**

Comment: This provision creates an easement in favor of the grantor out of land conveyed by the grantor in the same instrument. Provisions for the separate creation and transfer of easements are set out in §§11.106-11.107.

Instead of "excepting," as used in this provision, many lawyers use "reserving." The two words are discussed in §11.73.

The exception in this provision is expressly referred to as an easement to negate its construction as an estate in fee. On the difference between easements that are personal (in gross) and those that are appurtenant, see §§11.67-11.69. On problems with easements generally, see §§11.43-11.77.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/11 Descriptions of Property/§11.106 2. Form: Transfer of Appurtenant Easement

§11.106 2. Form: Transfer of Appurtenant Easement

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§11.105-11.107.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

11.106-1 Transfer of appurtenant easement

_ _[*Describe property conveyed*]_ _**, together with an easement appurtenant to that property** _ _[*described as/as described in*]_ _ _ _[*specify property covered by easement or instrument in which it is described*]_ _**.**

Comment: This provision transfers an appurtenant easement together with the land that it serves. Matters to consider with easements are discussed in §§11.67-11.69. It is by far the best practice to expressly recite all appurtenant easements with a transfer of the dominant tenement. A transfer of the dominant tenement absent an expression of an intent to transfer the easement will pass the easement by implication (CC §1084) but subject to the limitations of obvious and permanent use of CC §1104. See *Kytasty v Godwin* (1980) 102 CA3d 762, 771, 162 CR 556. See also §§11.54-11.55. The physical boundaries of easements may be described in as many ways as are possible for interests in fee. See §§11.14-11.41.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/11 Descriptions of Property/§11.107 3. Form: Creation of Easement

§11.107 3. Form: Creation of Easement

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§11.105-11.107.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

11.107-1 Creation of easement

_ _[*Name of transferor*]_ _ _ _[*grants/quitclaims*]_ _ **to** _ _[*name of transferee*]_ _ _ _[*describe property covered by easement*]_ _ **as an easement** _ _[*in gross, personal to transferee/appurtenant to* _ _[*describe dominant tenement*]_ _]_ _ **for** _ _[*describe purpose*]_ _ **for** _ _[*state duration, e.g., in perpetuity, as long as used for road purposes*]_ _**.**

Comment: As distinguished from the provisions in §11.105 (reservation of easement in favor of grantor) and §11.106 (transfer of easement with property to which it is appurtenant), this provision is used to create a new easement.

On matters affecting the description of easements, see §§11.43-11.77.

© The Regents of the University of California

§11.108 4. Release of Easement

An easement may be extinguished by a written release or quitclaim given by the owner of the easement to the owner of the servient tenement. *Westlake v Silva* (1942) 49 CA2d 476, 121 P2d 872. However, release by one beneficiary does not affect the interests of the other beneficiaries of the servitude. See Restatement (Third) of Property: Servitudes §7.3, Comment b (2000). In its bilateral aspect, a release is distinct from abandonment, which is unilateral. See Restatement §7.4, Comment a. See also §11.62. The owner of the servient tenement should not concur in the release without first making certain that he or she is fully protected, *e.g.,* that unwanted structures erected by the easement owner are first removed or that the releasing owner will indemnify against claims that the easement continues in force. The owner's attorney should advise the owner to examine a current preliminary report and inspection of the premises.

© The Regents of the University of California

§11.109 D. Describing Multiple Parcels

Multiple parcels should be described individually. Blanket conveyances of all of a grantor's property in a county or in an area are disfavored. The specific legal descriptions should always be used so that no doubt about the grantor's intent could be inferred. It is conceivable that blanket descriptions could be used in quitclaim deeds intended to clear large tracts of land or clouds on the title, but the specific legal descriptions are still preferable.

© The Regents of the University of California

§11.110 E. Eliminating Water Problems

Problems in describing lands bordered by water (lakes, streams, tidewaters, sloughs) are difficult to recognize, and once recognized are difficult to solve. (The effect of water on land is discussed in §§11.81-11.86. This section covers drafting problems.) Generally, the descriptions should be the joint product of the lawyer, engineer, and title officer. The seller should not purport to grant more than he or she has. The buyer should make certain that the description gives him or her all that the seller can convey, if that is the parties' intention.

The most common kinds of water are discussed below. Different kinds of water present various drafting problems, but two basic cautions always apply: Before drafting the description, investigate to ascertain whether any changes have occurred since the previous transfer, and draft the description to secure for the appropriate party the benefits that may flow from these changes.

- **Tidewaters.** To eliminate doubt, the conveyance to the buyer should specify to what line the grant is made, even if the intent coincides with the statutory rule discussed in §11.82. Usually, however, there should be no attempt to substitute surveyors' or other measurements for the intended water boundary. Such a description could deprive the buyer of accretions that occurred before close of escrow and create ambiguity about later accretions. For definition of "accretion," see CC §1014.
- **Navigable lake.** In the absence of other circumstances, the rights of the grantor to the low-water mark are considered to be included in the conveyance. CCP §2077. To negate "other circumstances," the low-water mark should be specified in the description if that is what is intended. As with tidewaters, however, an attempt to define the low-water mark by substituting surveyors' courses may deprive the buyer of accretions or compel the buyer to go to court to establish a right to them.
- **Nonnavigable stream or lake.** Unless the grant indicates a different intent, the abutting owner takes to the middle or thread of the lake or stream. See §11.83. As with tidewaters and navigable waters, it is better to express the parties' intent than to leave the description to statutory interpretation. However, the expressed intent should leave open to the buyer the benefit of the statutory provisions discussed in §11.82.

© The Regents of the University of California

§11.111 F. Contract Provision for Expressing Covenants in Deed

Certain covenants, although expressed in the purchase and sale agreement, are merged in the deed and become unenforceable when the deed is recorded unless they are stated in the deed itself. See §4.109. To avoid this problem, it is possible to expressly require in both the agreement and the escrow instructions that the covenants be included in the deed. The best place for this clause is directly following the description, where it serves as a flag to the drafter when the description is copied in preparing the deed.

© The Regents of the University of California

G. Statutory Remedies

§11.112 1. Quiet Title

Code of Civil Procedure §§760.010-764.080 in their modern (post-1980) form provide a broad and practical remedy for title issues, including matters related to legal descriptions, land title, easements, encroachments, boundaries, and other matters involving legal or equitable rights, title, estates, liens, or other interests in real property.

The statute of limitations on an action to quiet title accrues on presentation of the adverse claim (*Crest Mar Owners Ass'n v Stapakis* (2007) 157 CA4th 1223, 69 CR3d 231), but does not run against a plaintiff in possession of the property (*Muktarian v Barmby* (1965) 63 C2d 558, 560, 47 CR 483).

© The Regents of the University of California

§11.113 2. Declaratory Relief

Code of Civil Procedure §1060 provides for declaratory relief regarding rights to property or with respect to the location of the natural channel of water courses.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/11 Descriptions of Property/§11.114 3. Good Faith Improver

§11.114 3. Good Faith Improver

Code of Civil Procedure §§871.1-871.7 provide for remedies for good faith improvement of lands, made under an erroneous belief because of mistake of law or fact as to ownership, and authorize a court, consistent with principles of substantial justice and unjust enrichment, to adjust the rights of owners, lessees, lienholders, and encumbrancers to land.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/11 Descriptions of Property/§11.115 4. Marketable Record Title

§11.115 4. Marketable Record Title

Civil Code §§880.020-887.090 provide remedies for clearing title of ancient mortgages and deeds of trust, claims to mineral rights, options, powers of termination, unperformed contracts for sale of real property, and abandoned easements. Those statutes also include provisions for preservation of interests.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/11 Descriptions of Property/§11.116 5. Expired Offers of Dedication

§11.116 5. Expired Offers of Dedication

Code of Civil Procedure §771.010 provides that offers of dedication made by map that are not accepted and recorded within 25 years after recordation of the map are conclusively presumed to be unaccepted. Code of Civil Procedure §771.020 provides authority for an action to clear title.

© The Regents of the University of California

§11.117 6. Destroyed Land Records

The McEnerney Act (CCP §§751.02-751.28) provides a specific remedy in rem to establish record title to land in the event of loss of public records.

© The Regents of the University of California

§11.118 VI. DESCRIBING PERSONAL PROPERTY

Transfers of real property commonly include personal property on the premises. For instance, residences are often sold with carpets, drapes, and appliances. Sales of furnished apartment houses or other commercial properties may include elaborate inventories of furniture, fixtures, merchandise, and accounts receivable. Farm properties may be sold with livestock, harvested crops, or stock in mutual water companies.

If there are only a few items of personal property, they may be listed in the purchase and sale agreement. Longer lists are usually attached as exhibits. If the inventories are so extensive that they cannot be readily ascertained or valued by a visual inspection, the parties often agree that an inventory will be taken in the future by their representatives. In this situation, the total price is left open, but a method of computing the price (such as book value) must be agreed on. For a discussion of describing personal property in the purchase and sale agreement, see §4.33. For a form of agreement transferring the assets of a going business, see Sales and Mergers of California Businesses, chap 11 (Cal CEB 2002).

In any event, the need for certainty in describing personal property is as great as it is in describing the real property. On uncertainty rendering a contract illusory, see California Real Property Remedies and Damages §4.19 (2d ed Cal CEB 2002). If the property itself is not described in the agreement, the method by which it can be ascertained and located must be clear. For examples of descriptions of specific goods, see Secured Transactions in California Commercial Law Practice §1.9 (2d ed Cal CEB 2001).

PRACTICE TIP: Some kinds of personal property present special problems. For example, the seller's interest in a neon sign may be no more than a leasehold interest. The buyer should check with the manufacturer or lessor whose name is on the sign. Vehicles may be subject to encumbrances, as shown on registration slips. On public notice of other security instruments, see Secured Transactions §§3.76-3.115. To prevent substitution of goods after taking inventory, some buyers insist on possession of the goods as soon as inventory is completed; others place an indelible mark (*e.g.,* by means of a steel die) on each item. This is generally unnecessary for equipment that can be described by serial number. On bulk transfers without change of possession, see CC §3440.

© The Regents of the University of California

12

Covenants of Title

Scott A. Sommer

I. INTRODUCTION §12.1
- A. The Recording Act §12.2
- B. Modern Use of Title Insurance §12.3

II. COVENANTS OF TITLE
- A. Contractual Covenants §12.4
- B. Implied Covenants in California Statutory Grant Deed (CC §1113) §12.5
- C. Covenant of Seisin and Good Title §12.6
- D. Covenant Against Encumbrances §12.7
- E. Covenant of Right to Convey §12.8
- F. Covenants of Quiet Enjoyment and Warranty §12.9
- G. Covenant for Further Assurance §12.10
- H. Lineal and Collateral Warranties §12.11
- I. Form: Warranty Deed Covenants §12.12

III. REMEDIES FOR BREACH OF TITLE COVENANTS
- A. What Constitutes Breach
  1. Of Covenant of Seisin and Right to Convey §12.13
  2. Of Covenant Against Encumbrances §12.14
  3. Of Covenant of Quiet Enjoyment §12.15
  4. Of Covenant for Further Assurance §12.16
  5. Of Covenant of Warranty §12.17
- B. Damages §12.18
- C. Parties
  1. Who May Claim §12.19
  2. Parties Liable §12.20
- D. Table: Statutes of Limitations §12.21

IV. AVOIDING EFFECT OF TITLE COVENANTS
- A. Quitclaim Deed §12.22
- B. "Restrained" Grant Deed §12.23

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/12 Covenants of Title/§12.1 I. INTRODUCTION

§12.1 I. INTRODUCTION

The subject of covenants of title is a traditional one, arising from common law and statute in California. The covenants of title that are addressed in this chapter arose before title guaranties first appeared in the late 1800s—and long before modern forms of title insurance became widespread in the 1940s. Nevertheless, attorneys must understand this area of real property law to properly draft and review purchase and sale documentation, leases, and other instruments. The remedies for breach of these covenants, found in CC §§3304-3306, are sometimes available to complement other remedies for breach of contract, breach of warranty, and misrepresentation.

A covenant of title is "a covenant that binds the grantor to insure the completeness, security, and continuance of the title transferred. This covenant usually includes the covenants for seisin, against encumbrances, for the right to convey, for quiet enjoyment, and of warranty." Black's Law Dictionary 393 (8th ed 2004). Covenants of title can be placed in two groups:

- The covenants of seisin and good title (see §12.6), against encumbrances (see §12.7), and of the right to convey (see §12.8), which lie between parties in privity and do not run with the land; and
- The covenants of quiet enjoyment and warranty (see §12.9) and for further assurance (see §12.10), which do run with the land.

The law of covenants of title is codified in CC §§1113 and 1460-1468 and in case law. Certain special covenants of a lessor concerning contiguous property are in CC §§1469-1470.

Covenants of title are different from certain covenants of use that attach to title, run with the land, and are specially created under CC §1468. Section 1468 is the provision under which declarations of covenants, conditions, and restrictions are made binding on successive owners of the land and are of substantial modern interest. See §11.7.

Covenants of title should also not be confused with other contractual covenants that may be present in the real property contract, or with the express or implied warranties that may arise. The implied warranty of merchantability in new construction (*Pollard v Saxe & Yolles Dev. Co.* (1974) 12 C3d 374, 115 CR 648) is also distinct. Modern environmental liability under the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA) (42 USC §§9601-9675), the Carpenter-Presley-Tanner Hazardous Substance Account Act (HSA) (Health & S C §§25300-25395.15), and other environmental statutes can follow the chain of title but is unrelated to any covenant of title, although special covenants of indemnity in environmental matters can be made to run with the land as long as the formalities of CC §1468 or §1471 are observed. Restrictions created by ordinance are distinct from privately created covenants. *Elysian Inv. Group v Stewart Title Guar. Co.* (2002) 105 CA4th 315, 323, 129 CR2d 372.

For further discussion of covenants, conditions, and restrictions, see Advising California Common Interest Communities, chap 7 (Cal CEB 2003).

© The Regents of the University of California

§12.2 A. The Recording Act

Although a grantor or trustor may have granted an interest in property that would constitute a breach of the covenants in CC §1113 (see §§12.5-12.7), a bona fide purchaser for value without notice or a bona fide encumbrancer without notice will not be charged with the effect of such an interest unless constructive notice of the interest has been imparted within the meaning of the Recording Act (CC §§1213-1220) or unless the grantee of the prior interest was in possession at the time the subsequent grantee or mortgagee acquired title, thus imparting constructive notice of the prior conveyance. CC §19; *Scheerer v Cuddy* (1890) 85 C 270, 273, 24 P 713; *Marriage of Cloney* (2001) 91 CA4th 429, 437, 110 CR2d 615; *Triple A Mgmt. Co. v Frisone* (1999) 69 CA4th 520, 81 CR2d 669.

Civil Code §1214 provides that every conveyance of real property (see definition in CC §1215) is void as against any subsequent purchaser or mortgagee of the same property or any part of it in good faith and for valuable consideration, whose conveyance is first duly recorded. Recordation must be as prescribed by CC §1213, which requires that the document be acknowledged, certified, and recorded, appropriately subscribed by the party whose real property is thereby affected or alienated, and properly indexed. Govt C §§27288-27290. If it is improperly indexed or otherwise not entitled to recordation, even if it is accepted by a recorder, the document is deemed unlocatable and is treated as though it was never recorded. *Rice v Taylor* (1934) 220 C 629, 633, 32 P2d 381; *Cady v Purser* (1901) 131 C 552, 558, 63 P 844; *Hochstein v Romero* (1990) 219 CA3d 447, 452, 268 CR 202; 5 Miller & Starr, California Real Estate §§11:18-11:19, 11:21 (3d ed 2000). See also Govt C §§27201, 27248, 27257.

© The Regents of the University of California

§12.3 B. Modern Use of Title Insurance

In recent decades, it has become nearly universal practice to obtain title insurance in all lending and acquisitions secured by real property. Virtually every institutional lender and all federally created mortgage corporations require title insurance loan policies in proper form, and modern lenders' policies are specifically tailored to meet their requirements. In California, it is also nearly universal for purchasers of real property to ultimately rely on issuance of a title insurance policy insuring their title, subject to acceptable exceptions.

Nevertheless, the availability of title insurance neither alters the existence and enforceability of covenants of title nor reduces the need for the transactional real property attorney to understand the effect and use of such covenants in purchase and sale or loan documents. Moreover, not all interests in land fall within title insurance coverage. The CLTA standard-coverage policies do not offer protection against most unrecorded interests. Even ALTA policies exclude from coverage certain unrecorded interests known to an insured but not known to or reported in writing to the title insurer. See §4.53. On CLTA and ALTA policies generally, see California Title Insurance Practice, chaps 6-8 (2d ed Cal CEB 1997). In such instances, the buyer may possess an enforceable claim for damages against the grantor for breach of a covenant of title even though the title insurer would decline coverage.

© The Regents of the University of California

II. COVENANTS OF TITLE

§12.4 A. Contractual Covenants

Once having accepted a deed to property covered by a purchase agreement, a buyer may not generally rely on covenants of title contained in the agreement unless they are also contained in the deed. This general rule does not apply if mistake, fraud, or invalidity affects the deed, nor does it affect matters collateral to the deed. *Palos Verdes Corp. v Housing Auth.* (1962) 202 CA2d 827, 21 CR 225. Otherwise, contractual covenants are merged in the deed (*i.e.,* lost unless expressed in the deed). See *Szabo v Superior Court* (1978) 84 CA3d 839, 148 CR 837.

This chapter assumes, therefore, that the title covenants under discussion are contained in deeds. The fact that title covenants are in the deed does not negate the utility of covenants in the agreement. On the contrary, the agreement should contain all the title covenants that the parties expect the deed to contain. In addition, because covenants are merged in the deed unless a clear intent to the contrary is shown, the covenants should be specifically expressed in the deed unless the law implies them without express provision. Alternatively, the agreement may provide that a cause of action for breach of a covenant shall survive close of escrow and the conveyance of title and shall be enforceable in contract. See *Szabo v Superior Court, supra*. On covenants implied by the word "grant," see §§12.5-12.7; on contractual provisions for covenants and warranties to survive the deed, see §4.96.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/12 Covenants of Title/§12.5 B. Implied Covenants in California Statutory Grant Deed (CC §1113)

§12.5 B. Implied Covenants in California Statutory Grant Deed (CC §1113)

Civil Code §1113 provides:

> From the use of the word "grant" in any conveyance by which an estate of inheritance or fee simple is to be passed, the following covenants, and none other, on the part of the grantor for himself and his heirs to the grantee, his heirs, and assigns, are implied, unless restrained by express terms contained in such conveyance:
>
> 1. That previous to the time of the execution of such conveyance, the grantor has not conveyed the same estate, or any right, title, or interest therein, to any person other than the grantee;
>
> 2. That such estate is at the time of the execution of such conveyance free from encumbrances done, made, or suffered by the grantor, or any person claiming under him.
>
> Such covenants may be sued upon in the same manner as if they had been expressly inserted in the conveyance.

The covenants implied by CC §1113 are discussed in §§12.6-12.7. These covenants are implied only if the conveyance (1) contains the word "grant," (2) passes an estate of inheritance or fee simple, and (3) contains no express terms of "restraint" (*i.e.,* a limitation or qualification of the covenant that would otherwise be implied). For further discussion of restraints, see §12.23.

The word "grant" is not sufficient to raise the implication if the deed is a gift deed (*Estate of Porter* (1903) 138 C 618, 72 P 173) or a quitclaim deed (*i.e.,* a deed passing whatever interest the grantor has, even a fee, but without any representation that he has any interest). *Southern Pac. Co. v Dore* (1917) 34 CA 521, 168 P 147. See §12.22 on quitclaim deeds. On actions for breach of covenant, see §§12.13-12.21.

© The Regents of the University of California

§12.6 C. Covenant of Seisin and Good Title

The covenant of seisin is that the grantor is the owner of the premises granted, and seized of a good and indefeasible estate of inheritance free and clear of all encumbrances. *McCormick v Marcy* (1913) 165 C 386, 388, 132 P 449. It is to be emphasized that the statutory covenant of CC §1113 (see §12.5) is somewhat narrower—namely, that the grantor has previously not conveyed the same estate or any right, title, or interest to anyone else, and that the estate is free from encumbrances done, made, or suffered by the grantor or anyone claiming under the grantor.

The covenant is personal and is broken at the moment it is made if the grantor in fact lacks ownership. *Salmon v Vallejo* (1871) 41 C 481, 484. The cause of action does not run with the land and may be brought only by the covenantee. *Lawrence v Montgomery* (1869) 37 C 183, 188. The covenant is broken either by failure of the title or by an error in the acreage conveyed. *Salmon v Vallejo, supra*.

A buyer who wants the benefit of a covenant of seisin, either special or general, must make sure it is inserted in the deed. A provision for this covenant appears in §12.12. On negating the covenant, see §§12.22-12.23.

The covenant is not breached if the grantor conveys only the "right, title and interest" in the property (in modern terms, a quitclaim deed); in such a conveyance, nothing more passes than whatever estate the grantor had, subject to all present defects and equities. *Southern Pac. Co. v Dore* (1917) 34 CA 521, 523, 168 P 147.

The statute of limitations begins to run on a covenant of seisin, whether general or special, when the instrument is executed and the covenant broken. *Hotaling v Hotaling* (1924) 193 C 368, 379, 224 P 455; *McCormick v Marcy, supra*.

Covenants of seisin are sometimes used in the warranties and representations sections of purchase and sale agreements, but they are rarely expressed in the grant deed except through the word "grant." It is prudent to provide in the purchase and sale agreement that all representations, warranties, and covenants survive close of escrow and conveyance of title to the property. The buyer's primary reliance is usually on the following:

- The condition precedent that title insurance will be issued in a prescribed form subject only to the permitted exceptions; and
- The buyer's instructions to the escrow holder that escrow will not close until title insurance in the prescribed form is issued.

Usually, the title company issuing the policy is assumed to have greater financial responsibility than the grantor has in the event of a defect of title. Occasionally, however, it may be advisable for the buyer to obtain the grantor's covenant in addition to the title policy. On remedies for breach of covenant of seisin, see §§12.13, 12.18-12.20.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/12 Covenants of Title/§12.7 D. Covenant Against Encumbrances

§12.7 D. Covenant Against Encumbrances

The covenant against encumbrances, expressed in CC §1113(2) by the word "grant" in the conveyance of an estate of inheritance or fee simple, is "that such estate is at the time of the execution of such conveyance free from encumbrances done, made, or suffered by the grantor, or any person claiming under him."

Like the covenant of seisin (see §12.6), this covenant is personal and does not run with the land. *Salmon v Vallejo* (1871) 41 C 481; *Lawrence v Montgomery* (1869) 37 C 183; *Babb v Weemer* (1964) 225 CA2d 546, 37 CR 533. It is a special covenant, assuring only that the grantor has not encumbered the property or suffered it to be encumbered. It is not a covenant that the property is absolutely free of encumbrances unless contractually so expressed. The covenant does not depend on the grantor's actual knowledge; the grantor's prior knowledge or notice of an encumbrance is immaterial. *Evans v Faught* (1965) 231 CA2d 698, 709, 42 CR 133. The covenant is limited to encumbrances made by privately created covenant, not restrictions created by ordinance. *Elysian Inv. Group v Stewart Title Guar. Co.* (2002) 105 CA4th 315, 323, 129 CR2d 372.

An important distinction concerns encumbrances that involve physical character and that are open and notorious. Without an express agreement, the grantee is presumed to have contracted to accept the land subject to physical encumbrances of an open and notorious nature. The implied covenant against encumbrances under CC §1113 does not include visible easements or physical burdens on the land, even though they may also be of record. It does include matters that affect title, such as unrecorded leases, despite the grantee's knowledge of the tenant's interest. *Evans v Faught, supra*; *Sisk v Caswell* (1910) 14 CA 377, 112 P 185.

Modern usage of estoppel certificates from existing tenants and occupants arises from this rule. The rule is limited to situations that are inconsistent with record title. Possession by a tenant, consistent with recorded documents and without circumstances indicating that the tenant has additional rights, relieves the prospective buyer of a duty to inquire. *Caito v United Cal. Bank* (1978) 20 C3d 694, 702, 144 CR 751 (unrecorded lien of joint owner); *Gates Rubber Co. v Ulman* (1989) 214 CA3d 356, 262 CR 630 (unrecorded option to purchase, contained in lease, could not be enforced against grantee who took without notice of option).

The term "encumbrances" includes the following:

- Taxes, assessments, and liens on real property (CC §1114);
- Leases (*Evans v Faught, supra; Mann v Montgomery* (1907) 6 CA 646, 92 P 875);
- Mortgages, deeds of trust, judgment liens, attachments, water rights, easements, restrictions on use, or any right in a third party that diminishes the value or limits the use of the property, but is consistent with the passing of the fee (*Elysian Inv. Group v Stewart Title Guar. Co.* (2002) 105 CA4th 315, 320, 129 CR2d 372; see 3 Casner, American Law of Property §12.128 (1952); Hill, *Grant and the Obvious Encumbrance*, 41 LA B Bull 231 (1966)); and
- Nonpossessory interests such as a lien for unpaid taxes or even unpaid installments on an existing encumbrance (*Mains v City Title Ins. Co.* (1949) 34 C2d 580, 585, 212 P2d 873).

Under CC §1114, the term "encumbrances" is not limited to the definitions specifically furnished in the statute. *1119 Delaware v Continental Land Title Co.* (1993) 16 CA4th 992, 20 CR2d 438.

When a sale is made subject to a certain encumbrance, the purchaser may rely on a similar condition that it is free from any other one. *Mains v City Title Ins. Co., supra*; *Smiddy v Grafton* (1912) 163 C 16, 18, 124 P 433. The preferred practice is to insert words of restraint in both the agreement and the deed unless the escrow holder is instructed to pay all taxes that would otherwise be a lien. "Subject to" clauses are appropriate words of restraint if they appear in the deed. See the provision in §12.23.

The covenant is a promise to indemnify the grantee against loss; hence the grantee cannot recover until he or she has sustained a loss. *Wright v Boggess* (1914) 24 CA 533, 141 P 1082. The statute of limitations, however, begins to run when the covenant is made (*i.e.,* on delivery of the deed) and may well run before any loss has occurred. See *McPike v Heaton* (1900) 131 C 109, 63 P 179.

© The Regents of the University of California

§12.8 E. Covenant of Right to Convey

The covenant of the right to convey, although often held to be the equivalent of the covenant of seisin (see Comment in §12.12), is nevertheless a separate covenant. It may be used when the grantor does not own the property but has the right to convey it (*e.g.,* as attorney-in-fact for the owner). See Comment, *Covenants of Title Running With the Land in California*, 49 Cal L Rev 931, 934 (1961).

This covenant is not among those implied in the word "grant" under CC §1113. See §12.5. It is included in the provision in §12.12. It does not run with the land. See 49 Cal L Rev at 934. If the covenant is false, it is broken when made. California follows the rule that the chose in action is not assignable. *Salmon v Vallejo* (1871) 41 C 481.

© The Regents of the University of California

§12.9 F. Covenants of Quiet Enjoyment and Warranty

The covenant for quiet enjoyment is that the grantee will not be disturbed in possession because of a defective title. It is breached when the true owner evicts the buyer or asserts a paramount right such that the grantee, or the holder through the grantee, is compelled to yield possession or buy the outstanding title.

The statute of limitations accrues at the time of the eviction. *McCormick v Marcy* (1913) 165 C 386, 132 P 449. The covenants "of warranty" and "for quiet enjoyment" or for "further assurance" by the grantor run with the land by statute. CC §§1462-1463.

A warranty deed contains a covenant of warranty (Black's Law Dictionary 393 (8th ed 2004)), which is a promise that the covenantor will compensate the covenantee if the title to any part of the estate fails because of an outstanding paramount title in a third party. See *Tropico Land & Improvement Co. v Lambourn* (1915) 170 C 33, 38, 148 P 206. It is sometimes called a covenant of "non-claim." *Gee v Moore* (1859) 14 C 472, 473. As distinguished from covenants of seisin (see §12.6) and against encumbrances (see §12.7), covenants of warranty run with the land, but only when (CC §§1462-1463)

- contained in a deed; and
- made for the direct benefit of the property or some part of it then in existence.

The covenant for quiet enjoyment is essentially the same as the covenant of warranty. Both are intended to secure compensation to the buyer for a disturbance of quiet and peaceable possession if the buyer is evicted from the premises. See 3 Casner, American Law of Property §12.129 (1952). In contrast with the covenants of seisin, right to convey, and against encumbrances, which refer to the state of title and are broken if the defects exist, the covenants of warranty and for quiet enjoyment deal with the enjoyment of possession and are broken only when that enjoyment is disturbed. See 3 American Law of Property §12.129.

Warranty deeds are rarely used in California, although they are common in other parts of the country. There is no provision of law in California for a covenant of warranty except by express provision in the instrument. See §12.12 for such a provision.

PRACTICE TIP: From a buyer's point of view, it is usually better to rely on a secure title insurance company than on the seller's ability to respond in damages. A buyer can, however, have the benefit of both by negotiating for that protection as part of the purchase transaction. From a seller's point of view, a covenant of warranty should explicitly set forth the encumbrances to which the title is subject, in much the same manner as a title policy. For this purpose, the seller's attorney should be guided by a reliable and current preliminary report, but should add all unrecorded encumbrances of which the attorney or the client is aware. See Freshman, *The Warranty Deed: Where and When to Use It*, 51 LA BJ 186 (1975).

© The Regents of the University of California

§12.10 G. Covenant for Further Assurance

A covenant for further assurance is an undertaking by the seller to do any further acts to perfect the buyer's title that the buyer may reasonably require. *Wholey v Cavanaugh* (1891) 88 C 132, 135, 25 P 1112. This covenant carries with it a covenant against encumbrances, but it is substantially a covenant that the vendor will perform all acts necessary to confirm the buyer's title. Comment, *Covenants of Title Running With the Land in California*, 49 Cal L Rev 931, 936 (1961). Under CC §1463, it runs with the land in California if it otherwise complies with CC §§1462-1463.

The covenant for further assurance generally requires the grantor to convey after-acquired title to the grantee in order to give the grantee what he or she bargained for, but an express covenant for further assurance is not always necessary to protect the grantee. Thus, a grant in fee simple without an express covenant is sufficient to pass, by operation of law, the grantor's after-acquired title. CC §1106. A quitclaim deed transfers only the interest that the transferor has in the land at the date of its execution and thus does not carry an after-acquired title. *Johnson v E-Z Ins. Brokerage, Inc.* (2009) 175 CA4th 86, 94, 95 CR3d 782; *Taylor v Coachella Valley County Water Dist.* (1952) 108 CA2d 743, 239 P2d 454. Even though the doctrine of after-acquired title may apply to a given quitclaim deed (such as when the deed, expressly or impliedly, affirms the existence of a particular estate that the parties intended should pass by the conveyance), the covenant itself does not apply and would not be broken. *Estate of Wilson* (1940) 40 CA2d 229, 233, 104 P2d 716.

© The Regents of the University of California

§12.11 H. Lineal and Collateral Warranties

Although CC §1115 abolished "lineal and collateral warranties," it also provides that the heirs and devisees of someone who has made a covenant or an agreement in reference of, in, or to the title of any real property are answerable to the extent of the land descended or devised to them. Lineal warranties are rooted in early common law, and their modern effect, if any, is obscure. The abolition of the two principles by §1115 makes further consideration unnecessary.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/12 Covenants of Title/§12.12 I. Form: Warranty Deed Covenants

§12.12 I. Form: Warranty Deed Covenants

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

12.12-1 Warranty deed covenants

Grantor, for _ _[*himself/herself*]_ _ and _ _[*his/her*]_ _ heirs, representatives, and assigns, covenants with the grantee and _ _[*his/her*]_ _ heirs, representatives, and assigns, as follows:

[*Covenant of seisin*]

1. That grantor is lawfully seised _ _[*specify, e.g., in fee simple*]_ _ of the described property;

[*Covenant of right to convey*]

2. That grantor has the right to convey it;

[*Covenant of warranty and quiet enjoyment*]

3. That grantor warrants and will defend the title and quiet enjoyment of the property against the lawful claims and demands of all persons;

[*Covenant of further assurance*]

4. That grantor will do any further acts for the purpose of perfecting the title that the covenantees may reasonably require; and

[*Covenant against encumbrances*]

5. That the estate is free from all liens and encumbrances except _ _[*state exceptions*]_ _.

Comment: This provision contains all the title covenants designated in §12.5 and defined in §§12.6-12.10:

- Paragraph 1 is a covenant of seisin, which is used when the special covenant of seisin implied in CC §1113 is considered insufficient. The differences are explained in §12.6. This covenant will state, in effect, that the grantor is lawfully seised or has good and sufficient seisin. See 3 Casner, American Law of Property §12.127 (1952). However, because the rule in some states is that the simple covenant of seisin is not a representation or guaranty of the grantor's right or title (3 American Law of Property §12.127), the form makes the assurance explicit by stating that the grantor owns what he or she purports to convey.
- Paragraph 2 is a covenant of the right to convey, which is generally held to be the exact equivalent of a covenant of seisin, but it is used for a different purpose. However, because they are sometimes distinguished, both are expressed in this provision. The difference is explained in §12.8.
- Paragraph 3 combines the covenants of warranty and quiet enjoyment. These covenants are discussed in §12.9.
- Paragraph 4 is a covenant for further assurance, which is discussed in §12.10.
- Paragraph 5 is the covenant against encumbrances, discussed in §12.7. If the parties are satisfied with the special covenant provided by CC §1113, no broader covenant is required and this provision is unnecessary. If a general covenant is desired, a form like this may be used. In either case, liens or encumbrances to which the property will remain subject at the close should be expressly excluded from operation of the covenant. Unrecorded leases that an inspection would reveal limit the buyer's title, but, despite the buyer's knowledge, they breach the seller's implied covenant against encumbrances under §1113. *Evans v Faught* (1965) 231 CA2d 698, 710, 42 CR 133. The need to make the transfer subject to the lien of taxes or assessments is discussed in §12.7. Other exclusions frequently required are the following:
- Mortgages or deeds of trust to which the property remains subject;

- Utility easements;
- Leases; and
- Deed restrictions (CC&Rs).

Other exclusions (*e.g.,* impairment of marketable title, discussed in §4.51) may be required in a particular situation. An example of how to list these exceptions is provided in §12.23. It may be prudent to address restrictions created by ordinance if the grantor knows that the grantee's plans for the property may be affected. See *Elysian Inv. Group v Stewart Title Guar. Co.* (2002) 105 CA4th 315, 323, 129 CR2d 372.

Covenants in the purchase and sale agreement that are to survive the deed should also be in the deed. The agreement's provision against merger (see discussion in §4.109) preserves the buyer's rights, and including the covenants in the deed permits subsequent purchasers to enforce them in an appropriate case, either as covenants running with the land or as equitable servitudes.

© The Regents of the University of California

III. REMEDIES FOR BREACH OF TITLE COVENANTS

A. What Constitutes Breach

§12.13 1. Of Covenant of Seisin and Right to Convey

Breach of the covenant of seisin depends on breach of either the broader contractual covenant of seisin (see §12.6) or the narrower statutory covenant of CC §1113 (see §12.5). The statutory covenant against prior conveyance is breached only if the failure of title is due to an act of the grantor, not someone else. *Gaffey v Welk* (1920) 46 CA 385, 189 P 300.

The covenant of seisin refers only to prior transfers of estates in the land. A license does not breach the covenant, because it is not an estate in land; rather, it is a right to occupy under the previous owner only. *Shaw v Caldwell* (1911) 16 CA 1, 115 P 941. A conveyance of a water right, however, is an interest in land. *Lyles v Perrin* (1901) 134 C 417, 66 P 472. The covenant refers not only to the land itself but also to all property appurtenant to it. 3 Casner, American Law of Property §12.127 (1952). The covenant is broken at the time of transfer.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/12 Covenants of Title/§12.14 2. Of Covenant Against Encumbrances

§12.14 2. Of Covenant Against Encumbrances

If the encumbrance is one affecting title, the covenant against encumbrances is broken at the time of transfer; the grantee's prior knowledge or notice of the encumbrance is immaterial. The rule enunciated in *Evans v Faught* (1965) 231 CA2d 698, 42 CR 133, applies to this covenant against encumbrances, and thus the covenant applies only to encumbrances affecting title. It does not apply if the alleged encumbrance consists of a physical burden on the land, permanent in character and of an open and notorious nature, which affects only the physical condition of the property. 231 CA2d at 709.

The issue of breach also turns on whether the broad contractual covenant or the narrow statutory covenant of CC §1113(2) applies. Section 1113(2), unlike the contractual covenant against encumbrances, does not apply to encumbrances that were on the property at the time the grantor acquired title. *Crist v Fife* (1919) 41 CA 509, 183 P 197.

Some encumbrances, if made or suffered by the grantor or if an express contractual covenant was breached, give rise to a claim for damages in the same way as a mortgage or lien. The following are examples:

- Judgment liens (*Waggle v Worthy* (1887) 74 C 266, 15 P 831);
- Restrictions on use (*Fraser v Bentel* (1911) 161 C 390, 119 P 509);
- Building restrictions (*Tandy v Waesch* (1908) 154 C 108, 97 P 69);
- Easements (*Goldstein v Hensley* (1906) 4 CA 444, 88 P 507); and
- Unrecorded leases (*Evans v Faught, supra*).

© The Regents of the University of California

§12.15 3. Of Covenant of Quiet Enjoyment

Breach of the covenant for quiet and peaceable possession does not occur unless the true owner has evicted the buyer or asserted a paramount right. *McCormick v Marcy* (1913) 165 C 386, 389, 132 P 449. Because damages include attorney fees incurred in defending the title, the cause of action is normally deemed to accrue no later than the incurring of attorney fees for the true owner's assertion of a paramount right.

© The Regents of the University of California

§12.16 4. Of Covenant for Further Assurance

The covenant for further assurance requires the covenantor to take any further action to perfect the buyer's title that the buyer may reasonably require. See §12.10. Failure to do so within a reasonable time constitutes a breach. *Vance v Pena* (1871) 41 C 686. In contrast with covenants of warranty and of quiet enjoyment, which require only that the seller compensate the buyer if a third party has a superior title (see §12.9), this covenant requires the seller to take affirmative action against any third party. *Wholey v Cavanaugh* (1891) 88 C 132, 135, 25 P 1112.

© The Regents of the University of California

§12.17 5. Of Covenant of Warranty

The covenant of warranty is not breached until the buyer is evicted under paramount title. *Blackwell v Atkinson* (1859) 14 C 470. This occurs when there is actual eviction by process of law (*Norton v Jackson* (1855) 5 C 262, aff'd sub nom *Jackson v Norton* (1856) 6 C 187; *Fowler v Smith* (1852) 2 C 39, appeal at 2 C 568) or when the buyer or the buyer's successor is compelled to yield possession or buy the superior title (*McCormick v Marcy* (1913) 165 C 386, 389, 132 P 449).

© The Regents of the University of California

§12.18 B. Damages

Civil Code §3304 provides:

> The detriment caused by breach of a covenant of "seizin," of "right to convey," of "warranty," or of "quiet enjoyment," in a grant of an estate in real property, is deemed to be:
> 1. The price paid to the grantor; or, if the breach is partial only, such proportion of the price as the value of the property affected by the breach bore at the time of the grant to the value of the whole property;
> 2. Interest thereon for the time during which the grantee derived no benefit from the property, not exceeding five years;
> 3. Any expenses properly incurred by the covenantee in defending his possession.

Additional damages may be awarded to cover costs and attorney fees paid by the buyer in a prior action to recover the possession of which he or she was deprived by the seller's breach. *Levitzky v Canning* (1867) 33 C 299.

Civil Code §3305 provides:

> The detriment caused by the breach of a covenant against encumbrances in a grant of an estate in real property is deemed to be the amount which has been actually expended by the covenantee in extinguishing either the principal or interest thereof, not exceeding in the former case a proportion of the price paid to the grantor equivalent to the relative value at the time of the grant of the property affected by the breach, as compared with the whole, or, in the latter case, interest on a like amount.

Without alleging that he or she actually paid the encumbrance, the buyer may recover only nominal damages. CC §3305. See *Woods v Bennett* (1919) 40 CA 34, 180 P 25. See also *Wright v Boggess* (1914) 24 CA 533, 141 P 1082 (no cause of action arises until grantee pays encumbrance).

Section 3305 applies only to encumbrances that may be satisfied by money payments. The damages recoverable for other encumbrances (*e.g.,* restrictions or leases) are determined under breach of contract rules and are measured by the reduction in market value resulting naturally and proximately from the existence and the continuance of the encumbrance. CC §3300; *Fraser v Bentel* (1911) 161 C 390, 119 P 509; *Evans v Faught* (1964) 225 CA2d 546, 37 CR 533. But see *Babb v Weemer* (1965) 231 CA2d 698, 42 CR 133, indicating in dictum that no damages were recoverable when the grantee knew of the encumbrance, which was taken into account in setting the price.

© The Regents of the University of California

C. Parties

§12.19 1. Who May Claim

Who may recover for breach of a title covenant depends in part on whether the covenant runs with the land.

Covenants of seisin and good title, of the right to convey, and against encumbrances do not run with the land; only the buyer may bring action for their breach. See Comment, *Covenants of Title Running With the Land in California*, 49 Cal L Rev 931 (1961). Some judicial attempts have been made to extend the benefits of covenants of seisin and against encumbrances beyond the immediate buyer. See 49 Cal L Rev at 943.

Covenants of warranty, for quiet enjoyment, and for further assurance run with the land. The buyer as well as the buyer's successors may bring an action. CC §§1462-1463. Moreover, CC §1463 states that the buyer's covenant for the payment of taxes or assessments runs with the land, although it is likely that the framers of the statute had in mind only covenants made by lessees. The remote grantee's damages appear to be determined under CC §3304 and are limited to the price paid the original grantor, plus interest and expenses. *McCormick v Marcy* (1913) 165 C 386, 390, 132 P 449.

© The Regents of the University of California

§12.20 2. Parties Liable

The covenantor is liable to the covenantee on the title covenant whether or not the covenant runs with the land. *Barrows v Jackson* (1952) 112 CA2d 534, 247 P2d 99, aff'd (1953) 346 US 249, 97 L Ed 1586, 73 S Ct 1031. The covenantor is also liable to anyone to whom the buyer expressly assigns the benefits of the covenant (CC §§954, 1458) and is liable to remote grantees if the covenant runs with the land, even without an express assignment (CC §1460).

Aside from the covenantor, the only persons who are liable on the covenant are those who acquire the covenantor's whole estate in all or part of the property (CC §1465), if the covenant runs with the land (see CC §1460), and the covenantor's heirs and devisees to the extent of the land descended or devised to them (CC §1115).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/12 Covenants of Title/§12.21 D. Table: Statutes of Limitations

§12.21 D. Table: Statutes of Limitations

Actions for breach of title covenants are contract actions subject to the 4-year statute of limitations of CCP §337. The time when the statute begins to run depends on the nature of the covenant. The times for the respective covenants discussed in §§12.6-12.10 are summarized here:

Covenant	*Time Begins When*
Against encumbrances	Covenant is made
Of right to convey	Covenant is made
Of quiet enjoyment	Buyer or successor is evicted or compelled to buy the superior title, whichever occurs first
Of warranty	Buyer or successor is evicted or compelled to buy the superior title, whichever occurs first
For further assurance	Buyer or successor is evicted or covenantor or his or her successor fails to comply with a reasonable demand, whichever occurs first

© The Regents of the University of California

IV. AVOIDING EFFECT OF TITLE COVENANTS

§12.22 A. Quitclaim Deed

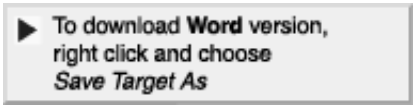
A seller wishing to avoid liability under title covenants may deliver a quitclaim deed to the buyer. This deed contains no express or implied warranties about the seller's title. It simply passes whatever interest, legal or equitable, the seller has at the time of conveyance. *Graff v Middleton* (1872) 43 C 341; *Klamath Land & Cattle Co. v Roemer* (1970) 12 CA3d 613, 618, 91 CR 112. However, a seller remains obligated to disclose to the buyer all facts materially affecting the value or desirability of the property that are known or accessible only to him or her and that are not known to or within the buyer's diligent attention and observation. *Lingsch v Savage* (1963) 213 CA2d 729, 735, 29 CR 201. The current residential disclosure form, codified in CC §1102.6, requires disclosure of "encroachments, easements or similar matters" and "CC&R's or other deed restrictions or obligations." See §6.36. Buyers sometimes do not want to accept a quitclaim, even when a title policy gives virtually every assurance needed. A quitclaim deed does not operate to transfer an after-acquired title. *Klamath Land & Cattle Co. v Roemer, supra*.

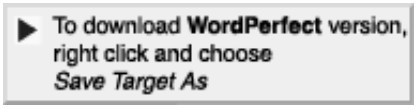
The deed obtained on a judicial sale is similar to a quitclaim deed and does not carry the covenants implied under CC §1113. See *Mains v City Title Ins. Co.* (1949) 34 C2d 580, 212 P2d 873. A probate sale, however, is not a judicial sale; the order is merely a confirmation, not an order for a judicial sale, and the buyer may rely on the implied covenants. *Mains v City Title Ins. Co., supra*.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/12 Covenants of Title/§12.23 B. 'Restrained' Grant Deed

§12.23 B. "Restrained" Grant Deed





A grant deed without express covenants carries with it no covenants other than the two implied in the word "grant." CC §1113; see §12.5. Even recognizing that the implied covenants are of scant protection to the buyer in most situations, the seller may nonetheless want to negate even that much liability. The seller can do so by giving a "restrained" grant deed. The most common way to accomplish this restraint is to set out in the grant deed the matters to which the title is subject, as in the example below.

***A* grants to *B* the following described property subject to the following:**

1. The lien of general and special city and county taxes for the fiscal year of July 1, 1998, to June 30, 1999;

2. Covenants, conditions, and restrictions of record;

3. Easement granted to Pacific Bell by deed recorded at _ _[*specify*]_ _;

4. Deed of trust to XYZ Title Company as Trustee, in which Charles White is beneficiary, recorded at _ _[*specify*]_ _; and

5. Unrecorded lease to National Stores, dated January 1, 1993, for a term from January 1, 1998, to December 31, 2010, containing an option for renewal for a term ending December 31, 2020, to be exercised before January 1, 2010, and an option to purchase the leased premises to be exercised before January 1, 2009.

A somewhat less common method incorporates a general disclaimer of covenants into the grant deed:

***A* grants to *B,* but without warranty or covenant of any kind, express or implied, the following described property: _ _[*List*]_ _.**

If the restraints consist of enumerating matters to which the title is subject, only items need be listed that would otherwise constitute breach under the implied covenants of CC §1113. These implied covenants are discussed in §§12.5-12.7.

EXAMPLE: Covenants, conditions, and restrictions of record need not be listed unless the seller personally, or anyone claiming under the seller, subjected the property or suffered it to be subjected to those restrictions. This omission is permitted because §1113 implies only a limited or special covenant.

Delinquent taxes or taxes for periods before close of escrow are usually prorated and charged to the seller, as discussed in §15.44 and the Comment to form 15.57-1.

Making a deed subject to a lease that contains an option to purchase may cloud the title for at least the period prescribed in the instrument, or the periods prescribed in CC §§715-719. The option may be shown as an exception in all preliminary reports and policies unless the title company is satisfied that §§715-719 protect it or unless the tenant releases the option or is barred by judgment from exercising it. See §8.16. For a recital to be used in removing a cloud created by inadvertence, see §10.43.

© The Regents of the University of California

13

Property Insurance

Timothy R. Sullivan

I. SCOPE OF CHAPTER; ATTORNEY'S ROLE §13.1

II. LOSS BEFORE TRANSFER OF TITLE: IS THE BUYER OR THE SELLER "ON THE RISK"? §13.2
- A. Liability Absent an Agreement: Uniform Vendor and Purchaser Risk Act (CC §1662) §13.3
- B. Material Loss Under CC §1662(a)
  - 1. Law in Absence of Agreement §13.4
  - 2. Form: Definition of "Material Loss" §13.5
- C. Who Bears Risk of Nonmaterial Loss Under CC §1662(a)
  - 1. Law in Absence of Agreement §13.6
  - 2. Form: Risk of Nonmaterial Loss §13.7
- D. Buyer's Assumption of Risk or Agreement to Insure
  - 1. Buyer's Possession Before Transfer of Title §13.8
  - 2. Form: Buyer's Assumption of Risk §13.9
  - 3. Form: Seller's Assumption of Risk §13.10
  - 4. Effect of Buyer's Agreement to Insure §13.11
  - 5. Negotiating Buyer's Agreement to Insure §13.12
- E. Form: Code Governs Except as Expressly Agreed §13.13
- F. Effect of Material Loss After Breach by Buyer §13.14

III. PERSONS WHO CAN INSURE THEIR INTEREST IN PROPERTY §13.15
- A. Insurable Interest §13.16
- B. Legal Title Is Not Required for an "Insurable Interest" §13.17
  - 1. Buyer §13.18
  - 2. Seller §13.19
  - 3. Lessee §13.20
  - 4. Mortgagee §13.21
  - 5. Remainderman §13.21A
- C. Insurable Interest Must Exist Both When the Policy Is Purchased and When the Loss Occurs §13.22
- D. Separate Interests Must Be Insured Separately §13.23
- E. Transfer of Seller's Insurance to the Buyer §13.24
- F. Reformation §13.25

IV. INSURING LENDERS AND MORTGAGORS
- A. Protecting Secured Lenders §13.26
- B. Loss Payable Clauses §13.27
  - 1. Simple Loss Payable Clause §13.28
  - 2. Standard Loss Payable Clause §13.29
- C. Effect of Insured's Fraud §13.30
- D. Credit Bids and Full Credit Bids
  - 1. Full Credit Bid Rule §13.31
  - 2. Credit Bid Rule §13.32

V. COMMON TYPES OF PROPERTY INSURANCE
- A. Noncommercial Property §13.33
  - 1. Fire §13.34
  - 2. Homeowners §13.35
  - 3. Dwellings §13.36
  - 4. Condominium Owners §13.37
- B. Commercial Property
  - 1. Building and Personal Property §13.38
  - 2. Businessowners Special Property §13.39
  - 3. Boiler and Machinery §13.40
  - 4. Theft, Disappearance, and Dishonesty §13.41

5. Robbery and Safe Burglary §13.42
6. Premises Burglary §13.43
C. Builders' Risk §13.44
D. Pollution §13.45
1. Pollution Legal Liability §13.46
2. Elements of Liability Defined §13.47
3. Exclusions From Liability §13.48
4. Cleanup Cost Cap §13.49
5. Property Transfer §13.50
6. Secured Lender or Secured Creditor §13.51
E. Earthquake Coverage §13.52
F. Flood Insurance §13.53
G. Ancillary Coverages for Commercial Risks §13.54
1. Business Interruption Coverage §13.55
a. Covered Causes of Loss §13.56
b. Optional Coverage for Interruption of Computer Operations §13.57
c. Described Premises §13.58
d. Total Suspension Versus Partial Interruption §13.59
e. Period of Restoration §13.60
f. Burden of Proof §13.61
g. Duty to Mitigate §13.62
h. Extra Expense §13.63
i. Rental Value §13.64
2. Other Ancillary Coverages
a. Computers and Electronic Equipment §13.65
b. Computer Fraud §13.66
c. Valuable Papers §13.67
d. Accounts Receivable §13.68

VI. HOW DO PROPERTY COVERAGES WORK?
A. "Covered Property" Versus "Property Not Covered" §13.69
B. Covered Causes of Loss §13.70
1. All Risks or All Perils §13.71
2. Named Risks or Named Perils §13.72
C. Direct Physical Loss §13.73
D. Exclusions §13.74
1. Exceptions §13.75
2. Who Has the Burden of Proof? §13.76
E. When Does a Loss Occur? §13.77
1. Episodic Loss §13.78
2. Continuous or Progressive Loss §13.79
a. Manifestation Rule §13.80
b. Fortuity §13.81
c. "Loss in Progress" Doctrine §13.82
3. Concurrent Causation and Efficient Proximate Cause §13.83

VII. COMMON EXCLUSIONS
A. Exclusions, Ensuing Losses, and Efficient Proximate Cause §13.84
B. List of Common Exclusions §13.85
1. Exclusions From Special Form (CP 10 30 04 02) §13.86
2. Exclusions From Special Form (CP 10 30 04 02) and Broad Form (CP 10 20 04 02) §13.87

VIII. WHAT TO DO WHEN A LOSS OCCURS: CONDITIONS
A. Notice to Insurance Company §13.88
B. Proof of Loss §13.89
C. Insured's Duty of Cooperation §13.90
D. Insurer's Duty to Produce "Claim-Related Documents" §13.91
E. Examination Under Oath §13.92
F. Statute of Limitations
1. 1-Year Limitations Period §13.93
2. Inception of the Loss §13.94
3. Tolling §13.95
4. Action "on the Policy" §13.96
G. Arbitration or Appraisal §13.97
H. California Residential Property Insurance Bill of Rights §13.98

IX. HOW IS THE LIABILITY CALCULATED: MEASURE OF INDEMNITY §13.99
A. Policy Limits
1. Amount of Coverage §13.100
2. "Open" Versus "Valued" Policies §13.101
B. Actual Cash Value §13.102
C. Replacement Cost Value §13.103
D. Guaranteed Replacement Cost §13.104
E. Extended Replacement Cost §13.105
F. Inflation Guard §13.106
G. Code-Mandated Repairs §13.107
H. Deductibles §13.108
I. Additional Requirements for Homeowners' Policies §13.109
J. Coinsurance Clauses §13.110
K. Value Reporting Clauses Regarding Inventory §13.111

X. WHEN THINGS GO WRONG: CLAIMS AGAINST THE INSURER
A. Common Law Bad Faith §13.112
B. Damages §13.113
1. Emotional Distress §13.114
2. Attorney Fees and Costs §13.115
3. Consequential Economic Loss §13.116
4. Punitive Damages
a. Clear and Convincing Evidentiary Standard §13.117
b. "Clear and Convincing" Evidence Is Required for Punitive Damages §13.117A
c. Corporate Entities May Be Held Liable for Punitive Damages Based on the Acts or Omissions of a "Managing Agent" §13.117B
d. Constitutionality of Punitive Damages §13.118
(1) First Guidepost: Reprehensibility of Defendant's Conduct §13.118A
(2) Second Guidepost: Disparity Between Harm Suffered by Plaintiff and Punitives Awarded §13.118B
(3) Third Guidepost: Court Review of Difference Between Punitives Awarded and Authorized Penalties **§13.1118C**
(4) Aggregate Disgorgement of Profits Theory Prohibited §13.118D
(5) Evidence of Defendant's Net Worth Required §13.118E
C. Duty of Good Faith Is Mutual; No Cause of Action for "Reverse Bad Faith" §13.119
D. Genuine Dispute Doctrine §13.120
E. No Cause of Action for Breach of Fiduciary Duty §13.121
F. Unfair Competition Claims Under Bus & P C §17200 §13.122
G. Other Statutory Violations §13.123

XI. EMERGING ISSUES REGARDING PROPERTY INSURANCE
A. Terrorism §13.124
1. All Commerical Insurers Must Participate **[Deleted]** §13.125
2. Commercial Insurers' Terrorism Exclusions Are Void **[Deleted]** §13.126
3. Characteristics of "Acts of Terrorism" **[Deleted]** §13.127
4. Certification by the Secretary of the Treasury **[Deleted]** §13.128
5. Types of New ISO Terrorism Exclusions **[Deleted]** §13.129
B. Mold §13.130
1. As a Covered Cause of Loss **[Deleted]** §13.131
2. Potentially Applicable Exclusions **[Deleted]** §13.132
C. Sick-Building Syndrome §13.133
1. Direct Physical Loss **[Deleted]** §13.134
2. Manifested During the Policy Term **[Deleted]** §13.135
3. Potentially Applicable Exclusions **[Deleted]** §13.136
D. Chinese Drywall §13.137
1. Direct Physical Loss §13.138
a. Odor; Release of Harmful Compounds §13.139
b. Safety and Habitability §13.140
2. Possible Applicable Exclusions §13.141

© The Regents of the University of California

§13.1 I. SCOPE OF CHAPTER; ATTORNEY'S ROLE

This chapter provides an overview of the common types of property insurance available to the buyer or the seller in a real property transfer. It is beyond the scope of this chapter to discuss these coverages in detail.

Knowledge of available types of insurance may be essential in successfully closing a real property transfer. For example, if the deal is jeopardized by the buyer's fear that the property might be contaminated, property transfer insurance or cleanup cost cap insurance (see §13.49) may make the risk acceptable and rescue the deal. In any event, even if a party's lawyer is sufficiently knowledgeable about insurance to recognize those issues in which it may play a role, the lawyer should delegate primary responsibility for selection of coverages to an experienced insurance agent or broker.

For a more detailed discussion of property insurance, see Insurance Claims for Property Loss: Determining Coverage and Presenting Claims (Cal CEB Action Guide Winter 2004).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.2 II. LOSS BEFORE TRANSFER OF TITLE: IS THE BUYER OR THE SELLER 'ON THE RISK'?

§13.2 II. LOSS BEFORE TRANSFER OF TITLE: IS THE BUYER OR THE SELLER "ON THE RISK"?

Once the parties enter into a contract to sell real property, the seller holds legal title as security for the unpaid purchase price, and the buyer has an equitable right to compel specific performance upon paying the purchase price. CC §1662. However, if property is damaged or destroyed before the sale is complete, issues can arise regarding whether the buyer must go through with the purchase, and who must bear the loss. The answers depend on whether the purchase agreement contains any express provisions addressing these issues.

© The Regents of the University of California

§13.3 A. Liability Absent an Agreement: Uniform Vendor and Purchaser Risk Act (CC §1662)

The Uniform Vendor and Purchaser Risk Act (CC §1662), adopted in California in 1947, was meant to eliminate doubt about when the risk of loss shifted from the seller to the buyer. See Comment, *Uniform Vendor and Purchaser Risk Act*: *Effect on California Law*, 36 Cal L Rev 476, 477 (1948). See also Fineberg, *Risk of Loss in Executory Contracts for the Sale of Real Property*, 14 Colum J L & Soc Probs 453, 464 (1979). California is one of 13 states that have adopted the Act. If the purchase and sale agreement does not address the risk of loss during the executory period, the Act controls. In general, when all or a material part of the subject property is destroyed without fault of either party after execution of the sales contract but before title has passed to the buyer, the seller's performance is excused and the buyer is entitled to the return of any consideration paid. The buyer is not entitled to specific performance with a reduction of the purchase price. *Dixon v Salvation Army* (1983) 142 CA3d 463, 191 CR 111.

Civil Code §1662 provides:

> Any contract hereafter made in this State for the purchase and sale of real property shall be interpreted as including an agreement that the parties shall have the following rights and duties, unless the contract expressly provides otherwise:
>
> (a) If, when neither the legal title nor the possession of the subject matter of the contract has been transferred, all or a material part thereof is destroyed without fault of the purchaser or is taken by eminent domain, the vendor cannot enforce the contract, and the purchaser is entitled to recover any portion of the price that he has paid;
>
> (b) If, when either the legal title or the possession of the subject matter of the contract has been transferred, all or any part thereof is destroyed without fault of the vendor or is taken by eminent domain, the purchaser is not thereby relieved from a duty to pay the price, nor is he entitled to recover any portion thereof that he has paid.
>
> This section shall be so interpreted and construed as to effectuate its general purpose to make uniform the law of those states which enact it.

The Act specifies when the buyer can recover what has been paid (§1662(a)) and when the seller can enforce the purchase and sale agreement against the buyer (§1662(b)). However, the Act does not specifically address insurance, or use the terms "risk" or "risk of loss." Nevertheless, if the seller cannot enforce the agreement, the seller cannot expect the buyer to pay for a material loss. Under §1662, unless the agreement provides otherwise, the party in possession bears the risk of loss before the transfer of legal title. *Long v Keller* (1980) 104 CA3d 312, 163 CR 532. Thus, an unexpected problem can arise for the buyer who is in possession as a tenant and then signs a purchase agreement or exercises an option in the lease. On execution of the agreement or exercise of the option, unless the documents provide otherwise, the risk of loss falls on the buyer (the tenant in possession), who frequently does not obtain property insurance until the close of escrow.

© The Regents of the University of California

B. Material Loss Under CC §1662(a)

§13.4 1. Law in Absence of Agreement

The risk of loss related to the property may be allocated between the parties in the purchase and sale agreement. See §§4.137-4.139 for a discussion of risk allocation in a purchase and sale agreement. The agreement, however, may be silent about which party bears the risk of loss, in which case CC §1662 (the Uniform Vendor and Purchaser Risk Act; see §13.3) will apply. The parties can also specifically state in the agreement that the Act will apply.

Civil Code §1662(a) states that the seller cannot enforce the purchase agreement if all or a material part of the property is destroyed when neither title nor possession has been transferred. The Act fails, however, to define "material." To avoid the uncertainties and expense of litigation over what constitutes a material loss, a purchase and sale agreement that apportions risk on the basis of the statute should include a definition as set forth in §13.5.

PRACTICE TIP: The amount of damage that will make the loss material is best expressed in a dollar amount rather than as a percentage of loss or destruction. The amount of damage from destruction should be stated as the cost of repair or replacement. Because the damage amount may vary if depreciation is considered, the agreement should specify whether depreciation will be used in making the calculation.

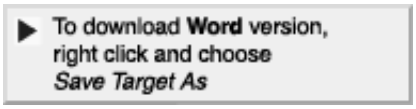
NOTE: In evaluating whether a loss by eminent domain is material, it is impractical to use the cost of repair or replacement. Reduction in market value is a better measure because it takes into account inverse condemnation and other factors affecting the value of the remaining parcel.

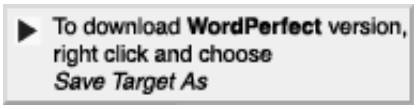
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.5 2. Form: Definition of 'Material Loss'

§13.5 2. Form: Definition of "Material Loss"

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§13.5-13.13.





13.5-1 Definition of "material loss"

For purposes of this agreement and for the application of California Civil Code §1662(a) to the extent that it applies, a destruction is material if the cost of repairing or replacing it, without deduction for depreciation, exceeds the sum of _ _[*dollar amount*]_ _, provided that if the applicable building codes or other laws or regulations require work exceeding the repair or replacement of the actual damage, the cost shall be considered to include all the work. A taking by eminent domain is material if the diminution in market value exceeds the sum stated above.

Comment: The purposes and effects of this provision are discussed in §13.4. For an example of a clause that is based on the intention of the parties and not on CC §1662, see §4.176 of the form purchase and sale agreement.

© The Regents of the University of California

C. Who Bears Risk of Nonmaterial Loss Under CC §1662(a)

§13.6 1. Law in Absence of Agreement

Civil Code §1662(a) applies only to situations in which all or a material part of the property is destroyed or taken by eminent domain (see §4.138). What happens if a nonmaterial loss occurs? Subsection (a) implies that the seller can still enforce the contract. If the seller does so, however, who pays for the damage?

Under CC §1662(a), the seller bears the risk of a material loss. Arguably, therefore, the seller should also bear the risk of a nonmaterial loss as long as he or she is in possession and presumably controls the property. See Fineberg, *Risk of Loss in Executory Contracts for the Sale of Real Property*, 14 Colum J L & Soc Probs 453, 470 (1979). This approach has been adopted in the New York version of the Uniform Vendor and Purchaser Risk Act, in which, if the loss is nonmaterial, the buyer, although compelled to perform the contract, is entitled to a reduction of the purchase price to the extent of the loss. New York General Obligations Law §5-1311.

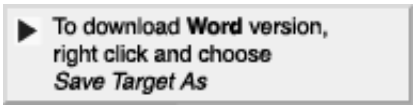
PRACTICE TIP: Because interpretation of the Uniform Vendor and Purchaser Risk Act is intended to be uniform, the courts might interpret CC §1662(a) to achieve the same result as provided expressly by the New York law. See 17 Williston on Contracts §50.50 (4th ed 1990). However, it is best to insert in the purchase and sale agreement a clause expressly providing that the seller bears the risk of a nonmaterial loss and that the purchase price is to be reduced to the extent of any loss. See §13.7.

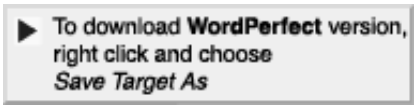
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.7 2. Form: Risk of Nonmaterial Loss

§13.7 2. Form: Risk of Nonmaterial Loss

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§13.5-13.13.





13.7-1 Risk of nonmaterial loss

If, when neither legal title nor possession of the subject matter of this contract has been transferred, a nonmaterial part of the subject matter is destroyed or is taken by eminent domain, neither Seller nor Buyer is thereby deprived of the right to enforce the contract; but, if the nonmaterial part is destroyed without the fault of the Buyer or is taken by eminent domain, the Buyer is entitled to a reduction of the purchase price to the extent of the cost of repairing or replacing the damage from destruction or the diminution in value resulting from eminent domain.

Comment: The need for this provision is explained in §13.6. See the saving clause in §13.13.

© The Regents of the University of California

D. Buyer's Assumption of Risk or Agreement to Insure

§13.8 1. Buyer's Possession Before Transfer of Title

The transfer of either title or possession shifts the risk of loss to the buyer. CC §1662(b); see §13.3. The point at which the risk shifts can, however, be altered in the purchase and sale agreement. See §§13.4-13.5. In most transactions, the buyer's insurance coverage, whether obtained by assuming the seller's insurance or by acquiring new insurance, does not take effect until close of escrow. In this situation, a buyer who takes possession before title passes is unprotected against the risk of loss unless the agreement places the risk on the seller until close of escrow. See *Long v Keller* (1980) 104 CA3d 312, 163 CR 532. A buyer who plans to take possession before title passes should make certain that coverage becomes effective on the date of possession rather than at the close of escrow, or should provide in the purchase and sale agreement that the seller retains the risk until title passes. See form 13.10-1. If the risk shifts to the buyer as a result of a provision in the agreement, the insurance should be made effective when the agreement is executed. For a provision assigning the risk to the buyer, see form 13.9-1.

If the buyer is to take over the seller's insurance, the buyer should require the seller to name the buyer as an additional insured in the seller's existing policy and to furnish a certificate of insurance within a specified time. The certificate should show the extent of the coverage and the fact that the buyer has been named as an additional insured. If the insurer resists adding the buyer or if the coverage is inadequate, the buyer should obtain new coverage. In most situations, the buyer is better advised to obtain a new policy so that coverage can be tailored to the buyer's specific needs.

NOTE: A certificate of insurance is not a contract with the insurer, and, if executed by a broker without authority, it will not bind the insurer. See Practice Tip in §13.23.

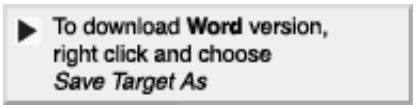
Even when the risk shifts to the buyer before the close of escrow, insurance protection is still a concern for the seller. Many policies provide that a change in interest or possession of the insured property will suspend the coverage. See Ins C §300; *Mackintosh v Agricultural Fire Ins. Co.* (1907) 150 C 440, 89 P 102; *Finkbohner v Glens Falls Ins. Co.* (1907) 6 CA 379, 92 P 318. To address this concern, agreements sometimes require the buyer to insure if the buyer is to take possession before title passes. See §13.11.

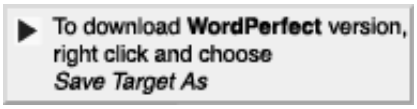
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.9 2. Form: Buyer's Assumption of Risk

§13.9 2. Form: Buyer's Assumption of Risk

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§13.5-13.13.





13.9-1 Buyer's assumption of risk

Buyer shall not, through eminent domain or the destruction of all or any part of the property without Seller's fault, be relieved of the obligation to complete the purchase. Buyer shall bear the risk of all losses by destruction without fault of Seller or by eminent domain.

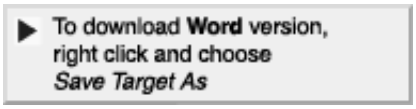
Comment: This provision shifts the risk of loss to the buyer on execution of the agreement and requires the buyer to purchase, despite any loss covered by CC §1662(a). Its utility is discussed in §13.8; for an additional caveat, see §13.12. See also form 4.176-1 on condemnation, in which the buyer has the option of proceeding with the purchase, and form 4.176-2 on damage and destruction.

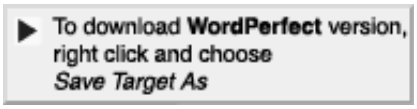
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.10 3. Form: Seller's Assumption of Risk

§13.10 3. Form: Seller's Assumption of Risk

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§13.5-13.13.





13.10-1 Seller's assumption of risk

If improvements on the property are destroyed or materially damaged before the close of escrow, Buyer shall be relieved of the obligation to complete the purchase. On demand of Buyer, any deposit made by Buyer shall be returned to Buyer.

Comment: This provision alters the risk of loss under the Uniform Vendor and Purchaser Risk Act (CC §1662) by delaying the shift of risk to the buyer until title passes to the buyer. This provision should be considered if the buyer is a tenant in possession or otherwise may take possession before close of escrow.

© The Regents of the University of California

§13.11 4. Effect of Buyer's Agreement to Insure

Does a requirement that the buyer maintain insurance constitute an "express" provision under CC §1662 (see §13.8) and therefore shift the risk to the buyer? The California courts have not yet addressed this question.

Cases decided before the enactment of CC §1662 indicate that an agreement to insure is evidence of an intent to assume the risk of loss. See *Ware v Security-First Nat'l Bank* (1936) 7 C2d 604, 61 P2d 936; *Kelly v Smith* (1933) 218 C 543, 24 P2d 471. In both cases, the buyer had the right of possession, but the court placed equal emphasis on the existence of the agreement to insure as evidence of an intent to assume the risk of loss. See 13 Witkin, Summary of California Law, *Equity* §§175-176 (10th ed 2005).

If the courts decide that an insurance clause is an express provision shifting the risk of loss under CC §1662, the following issues should be considered by a buyer who agrees to maintain insurance:

- If the loss exceeds the coverage, the buyer may have to pay the difference between the proceeds received from the insurance and the agreed price of the property. See Comment, *Uniform Vendor and Purchaser Risk Act*: *Effect on California Law*, 36 Cal L Rev 476, 478 (1948).
- The cost of insuring some risks (*e.g.,* earthquake and flood) is prohibitive.
- The insurer may resist the buyer's claim on the ground that the buyer lacks an insurable interest. See Ins C §286.
- The agreement should expressly state whether or not the risk of loss is intended to be shifted to the buyer.

On negotiating agreements to insure, see §13.12.

© The Regents of the University of California

§13.12 5. Negotiating Buyer's Agreement to Insure

In addition to the problems arising from an interpretation of the buyer's agreement to insure discussed in §13.11, a provision requiring the buyer to insure is extremely difficult to draft. The advice of a competent insurance broker or counselor may be helpful, and the requirements of the lender or prospective lender should be ascertained.

Several issues arise in deciding which perils are to be covered: It is seldom possible to anticipate every risk; the premiums for some risks may be considered prohibitive; and the descriptive names given to various policies or risks may be confusing to persons outside the field.

The amount of coverage is another problem. A fixed dollar amount may be appropriate in some situations; in others, it may be better to require coverage "for the full undepreciated value of the improvements" (or a variation of that language). See §13.100.

Because some insurance companies have had their financial ratings downgraded because of large losses and poor investment returns, lawyers should specify that the insurance must be carried by companies with certain ratings, such as those in A.M. Best's Insurance Reports.

Best has two ratings: One shows assets (from Class I, with assets of less than $250,000, to Class XV, with assets of $100 million or more). The other gives evaluations based on comparisons with peers and industry standards; evaluation of a company's balance sheet strength, operating performance, and business profile; and assessment of an insurer's operating plans, philosophy, and management. On the latter scale are the following gradings: A++/A+ (superior financial strength and ability to meet obligations to policyholders), A/A− (excellent), B++/B+ (very good), B/B− (fair), C++/C+ (marginal), and C/C− (weak).

Disposition of the proceeds in the event of loss may also be difficult to negotiate or draft. If title has not yet passed, the seller may be reluctant to see the proceeds go outright to the buyer. The buyer, on the other hand, may be eager to commence restoration before escrow closes. If the parties agree to entrust the funds to a trustee or an escrow holder, the agent's requirements must be ascertained and all contingencies must be anticipated (*e.g.,* disposition of the proceeds if the buyer defaults or exercises a permitted disapproval in the agreement).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.13 E. Form: Code Governs Except as Expressly Agreed

§13.13 E. Form: Code Governs Except as Expressly Agreed

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§13.5-13.13.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

13.13-1 Code governs except as expressly agreed

Except as expressly provided in _ _[*designate provisions relating to risk of loss or right to enforce after destruction or condemnation*]**_ _, this agreement shall be governed by California Civil Code §1662 in effect at the date of this agreement.**

Comment: At least one court has held that any provision on risk of loss makes the entire Uniform Vendor and Purchaser Risk Act inapplicable because the parties had provided otherwise. *World Exhibit Corp. v City Bank Farmers Trust Co.* (App Div 1946) 61 NYS2d 889, 893, aff'd (1946) 296 NY 586, 68 NE2d 876 (construing statute similar to CC §1662). To meet this problem, it is desirable to state that the Act will apply to the extent it does not conflict with the contract. For discussion of a clause that replaces the Act and states the parties' intentions, see §§4.137-4.139.

© The Regents of the University of California

§13.14 F. Effect of Material Loss After Breach by Buyer

Civil Code §1662(a) does not specify the effect of a material loss during a period when the buyer is in default. The decision in *Tinker v McLellan* (1958) 165 CA2d 291, 331 P2d 464, although not directly based on §1662(a), indicates that a buyer in default may not be able to avoid his or her obligation when the property is destroyed.

© The Regents of the University of California

§13.15 III. PERSONS WHO CAN INSURE THEIR INTEREST IN PROPERTY

The saying goes that if you pay enough, you can get insurance for anything. Golf tournaments offer a prize for hitting a hole-in-one, then buy insurance in case someone does. Jimmy Durante insured his nose for $50,000. Insurance coverage is available for cancellation of a wedding, for loss of a stallion's virility, or for alien abduction.

However, prospective insureds must risk losing something before they can insure that risk. If the insured has nothing to lose, the insurance contract is considered purely a wager that the risk will not occur. *Riley v Mid-Century Ins. Exch.* (1981) 118 CA3d 195, 199, 173 CR 257. For example, despite the risk of earthquake or other disaster, a person with no ownership or other pecuniary interest in the Bay Bridge could not purchase a valid insurance policy covering the Bridge. This is the concept of "insurable interest." See §13.16.

© The Regents of the University of California

§13.16 A. Insurable Interest

Although we commonly speak of a property as being insured, in reality property insurance does not insure the property itself, but insures the insured's interest in the property. *Davis v Phoenix Ins. Co.* (1896) 111 C 409, 414, 43 P 1115; *Burns v California Fair Plan* (2007) 152 CA4th 646, 651, 61 CR3d 809; *Royal Ins. Co. v Sisters of Presentation* (9th Cir 1970) 430 F2d 759, 761 (applying California law). To place a contract of insurance on an improvement and recover in the event of loss, one must have an "insurable interest" in the property. Ins C §280.

"Insurable interest" is a term of art that is defined broadly to include "every interest in property, or any relation thereto, or liability in respect thereof, if such in nature that a contemplated peril might directly damnify the insured." Ins C §281; *Davis v Phoenix Ins. Co.* (1896) 111 C 409, 414, 43 P 1115.

An insurable interest can be an "existing interest," an "inchoate interest founded on an existing interest," or an "expectancy, coupled with an existing interest… out of which the expectancy arises." Ins C §282. Thus, in certain circumstances, a future interest could be insurable. See, *e.g.*, *Burns,* 152 CA4th at 652 (both life tenant and remainderman have insurable interest in property). However, a mere contingent or expected interest in anything, if not founded on an actual right to the thing or on any valid contract for it, is not insurable. Ins C §283.

NOTE: No cases have interpreted a "mere contingent" or "expected interest" within the meaning of these statutes. However, CC §700 distinguishes between future interests and "possibilities." Under CC §700, "[a] mere possibility, such as the expectancy of an heir apparent, is not to be deemed an interest of any kind." This distinction may be relevant in interpreting Ins C §283.

© The Regents of the University of California

§13.17 B. Legal Title Is Not Required for an "Insurable Interest"

Legal title to property is not controlling for purposes of having an insurable interest (see §13.16); the existence of an insurable interest hinges on economic interests rather than naked legal title. *Royal Ins. Co. v Sisters of Presentation* (9th Cir 1970) 430 F2d 759, 762. A direct pecuniary interest in the preservation of the property, and a pecuniary loss as a result of its destruction, is both a sufficient condition (*Davis v Phoenix Ins. Co.* (1896) 111 C 409, 414, 43 P 1115) and a necessary one: Legal title in itself will not confer an "insurable interest" unless the title holder will suffer a pecuniary loss if the property is destroyed. For example, in *Royal Ins. v Sisters of Presentation*, *supra,* a convent of an order of nuns became so dilapidated that the city declared it to be uninhabitable. The nuns exchanged the convent parcel for an adjacent parcel on which their new convent was to be built. Under the exchange agreement, the old convent would be demolished and the land would be used by a high school. Before the old convent was demolished, it burned. The district court held the nuns had an insurable interest because they might have used the old convent if some calamity destroyed the new convent. Applying California law, the Ninth Circuit reversed, concluding that, despite holding title to the convent, the nuns suffered no pecuniary loss as a result of its destruction, and thus had no insurable interest at the time of the loss. Likewise, in *Smith v Jim Dandy Markets, Inc.* (9th Cir 1949) 172 F2d 616, the legal owner of a building sold all the equipment and supplies related to the building and leased the building itself. The Ninth Circuit, applying California law, held that the holder of the legal title had lost his insurable interest by operation of the contractual arrangements.

© The Regents of the University of California

§13.18 1. Buyer

The buyer has an equitable right to compel specific performance upon paying the purchase price. CC §1662. Although title has not yet passed, the buyer may be at risk in case of loss, depending on the risk-of-loss provisions of the contract and whether the Uniform Vendor and Purchaser Risk Act (CC §1662) applies. See §13.8. A buyer in possession under a contract who has paid part of the purchase price, and who will be entitled to conveyance of legal title upon completion of the contract, has an insurable interest equal to the amount of payments made. *Davis v Phoenix Ins. Co.* (1896) 111 C 409, 414, 43 P 1115.

© The Regents of the University of California

§13.19 2. Seller

Under an executory sales contract, the seller holds legal title as security for the unpaid purchase price. CC §1662. However, once property is sold, the seller retains no insurable interest absent a security interest. *Warner v Fire Ins. Exch.* (1991) 230 CA3d 1029, 281 CR 635; *Hoffman v State Farm Fire & Cas. Co.* (1993) 16 CA4th 184, 19 CR2d 809.

© The Regents of the University of California

§13.20 3. Lessee

A binding contract to assume obligations under a lease can create an insurable interest. See *California Food Serv. Corp. v Great Am. Ins. Co.* (1982) 130 CA3d 892, 897, 182 CR 67. Similarly, liability for property owned by another can create an insurable interest. *Shade Foods, Inc. v Innovative Prods. Sales & Mktg., Inc.* (2000) 78 CA4th 847, 875, 93 CR2d 364.

© The Regents of the University of California

§13.21 4. Mortgagee

The interest created by a mortgage or deed of trust is an insurable interest distinct from that of the mortgagor or grantor. *Alexander v Security-First Nat'l Bank* (1936) 7 C2d 718, 62 P2d 735; *Martin v World Sav. & Loan Ass'n* (2001) 92 CA4th 803, 806, 112 CR2d 225; *Mosee v Firemen's Fund Ins. Co.* (1927) 87 CA 473, 475, 262 P 436; *Davis v Phoenix Ins. Co.* (1896) 111 C 409, 43 P 1115.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.21A 5. Remainderman

§13.21A 5. Remainderman

Both a life tenant and a remainderman have an insurable interest in property in which a life interest and a future interest have been created. *Burns v California Fair Plan* (2007) 152 CA4th 646, 61 CR3d 809.

© The Regents of the University of California

§13.22 C. Insurable Interest Must Exist Both When the Policy Is Purchased and When the Loss Occurs

The insurable interest must exist when the policy takes effect and when the loss occurs. Between those two points, however, the interest need not exist. Ins C §286; *Banerian v O'Malley* (1974) 42 CA3d 604, 614, 116 CR 919.

In *Hoffman v State Farm Fire & Cas. Co.* (1993) 16 CA4th 184, 19 CR2d 809, the insureds' home was located within a landslide area. After they sold their home, they made a claim under their homeowner's insurance. Although the insureds alleged that no damage to their home manifested itself before the sale, they claimed they received a lower price because damage to homes on the other side of the landslide area depressed the value of their home. They further alleged that damage to their home manifested itself over a year after they sold it. The appellate court held that the insureds had no insurable interest in the property at the time of the manifestation of the loss, and thus could not state a claim against the insurer.

© The Regents of the University of California

§13.23 D. Separate Interests Must Be Insured Separately

Several persons or entities may have insurable interests in property at the same time, such as a seller and buyer (*Long v Keller* (1980) 104 CA3d 312, 316, 163 CR 532); joint owners (*Russell v Williams* (1962) 58 C2d 487, 490, 24 CR 859); a mortgagor and mortgagee (*Foothill Village Homeowners Ass'n v Bishop* (1999) 68 CA4th 1364, 1373, 81 CR2d 195); a condominium owner and a homeowners association, who both have interests in the condominium's common areas (*Chateau Chamberay Homeowners Ass'n v Associated Int'l Ins. Co.* (2001) 90 CA4th 335, 340, 108 CR2d 776); or a life tenant and a remainderman (*Burns v California Fair Plan* (2007) 152 CA4th 646, 652, 61 CR3d 809). However, even if multiple parties have insurable interests, no party has an interest in insurance obtained by the others. *Long,* 104 CA3d at 316.

Regardless of policy limits, an insured can recover only up to the amount of his or her insurable interest in the property. Ins C §284; *Whitney Estate Co. v Northern Assur. Co.* (1909) 155 C 521, 101 P 911; *Burns v California Fair Plan, supra*. Thus, in cases of multiple ownership, all parties should be named.

The persons or entities listed on the declarations page of the policy are the named insureds. Other persons or entities with insurable interests in the property may be listed as additional insureds. Typically, lenders require that the borrower obtain insurance and that they be named as additional insureds.

PRACTICE TIP: Lenders often require the owner to provide them with a certificate of insurance indicating that the lender has been added as an additional insured on the policy purchased by the owner. However, while a certificate of insurance is evidence of insurance, it is not a contract between the insurer and the certificate holder. *Pardee Constr. Co. v Insurance Co. of the W.* (2000) 77 CA4th 1340, 1347 n2, 92 CR2d 443. The certificate is issued by a broker or agent, not by the insurer. This poses the risk that the broker or agent will fail to confirm that the policy is amended to name the additional insured, or that the insurer will refuse to do so. An insurer will be obligated, however, to afford coverage for the certificate holder even if the policy has not been amended, if the certificate was issued by an authorized agent or an agent with ostensible authority. *American Cas. Co. v Krieger* (9th Cir 1999) 181 F3d 1113, 1121. Rather than risk a dispute regarding the agent's authority, the more prudent approach is for the additional insured to obtain a copy of the actual policy endorsement adding it as an additional insured.

© The Regents of the University of California

§13.24 E. Transfer of Seller's Insurance to the Buyer

In addition to protection against loss pending the transfer of title (see §§13.2-13.13), the buyer needs protection against loss from destruction of the property after title passes. The buyer may obtain protection by purchasing new insurance or by taking an assignment of the seller's insurance. Generally, it is better for the buyer to obtain new insurance.

If the buyer expects to take over the seller's insurance, an express transfer of the policy is necessary because insurance policies on real property do not pass with the title on the sale of the property insured. *Alexander v Security-First Nat'l Bank* (1936) 7 C2d 718, 62 P2d 735. Under Ins C §305, the "mere transfer of subject matter insured does not transfer the insurance, but suspends it until the same person becomes the owner of both the insurance and the subject matter insured."

This rule follows from the principle that the property contract does not insure the property itself but rather the named insured's interest in that property. See §13.16. However, a transfer of interest between jointly insured joint owners, such as partners, joint tenants, or tenants in common, does not void the insurance, even if the policy states that the insurance shall cease on alienation of the property. Ins C §304.

A change of ownership without a corresponding change in the named insureds on the contract suspends coverage until the change in the named insureds is made. Ins C §§300, 305. When the change is not made and a loss occurs, however, courts of equity may provide relief. See §13.25.

Even when the insurance policy does not expressly limit its assignability, the courts have held that the insurer's consent must be obtained for an express assignment of the policy. *Bergson v Builders Ins. Co.* (1869) 38 C 541, 543.

The courts will not invalidate a hazard insurance policy, despite its assignment without the insurer's consent before the loss, as long as the insurer suffered no prejudice from lack of notice and would have consented if notice had been given, and if invalidation of the policy would result in forfeiture. *University of Judaism v Transamerica Ins. Co.* (1976) 61 CA3d 937, 132 CR 907.

Under the California Standard Form Fire Insurance Policy as set forth in Ins C §2071, assignment of the policy is invalid without the insurance company's written consent. Although fire insurance policies on California property need not be written on the standard form policy if the coverage against fire loss is substantially equal or more favorable to the insured than that of the standard form policy (Ins C §2070), most policies contain most of the provisions of the standard form. Despite the requirement of written consent to assignment in the standard form, however, the insurer may waive consent (*Limsky v Scottish Union & Nat'l Ins. Co.* (1924) 68 CA 688, 229 P 1017; *Lewis v Reed* (1920) 48 CA 742, 192 P 335) or estop itself to deny that consent was given (*Tucker v American Ins. Co.* (1932) 123 CA 316, 11 P2d 55). Express consent is, of course, better assurance to the buyer.

PRACTICE TIP: Ordinarily, the details of obtaining consent from the insurance company are handled through the real estate broker or the insurance broker. Insurance companies use a standard form providing for the assignment.

The requirement of the insurer's consent to an assignment does not apply to assignments after a loss. Any right of the insured to insurance proceeds resulting from loss may be assigned without the consent of the insurer. Ins C §520; *Greco v Oregon Mut. Fire Ins. Co.* (1961) 191 CA2d 674, 12 CR 802; *Vierneisel v Rhode Island Ins. Co.* (1946) 77 CA2d 229, 175 P2d 63.

© The Regents of the University of California

§13.25 F. Reformation

If an insurance policy does not reflect the correct name of the owner of the property as a result of fraud or mistake, the policy may be reformed to reflect the correct name. *Gillis v Sun Ins. Office, Ltd.* (1965) 238 CA2d 408, 47 CR 868. However, a policy will not be reformed based on the insured's unilateral mistake if the insurer did not know about or suspect that the insured had made a mistake. *Bonaparte v Allstate Ins. Co.* (9th Cir 1994) 49 F3d 486, 488; CC §3399.

© The Regents of the University of California

IV. INSURING LENDERS AND MORTGAGORS

§13.26 A. Protecting Secured Lenders

The interest of the secured lender should be protected by insurance on the property that secures the debt. It was once common for lenders to require insureds to purchase insurance in an amount equal to the loan balance, even when it substantially exceeded the replacement cost of the structure. However, CC §2955.5(a) now prohibits lenders from imposing such a requirement. Lending institutions do require that the insurance proceeds be payable to the lender to the extent of its interest. See *Martin v World Sav. & Loan Ass'n* (2001) 92 CA4th 803, 112 CR2d 225. This protection is especially important in a California purchase money deed of trust given to the seller (or, in the case of an owner-occupied, one-to-four-unit dwelling, given to a third party lender), because the value of the property represents the lender's sole security and source of repayment in a default. CCP §580b; *Krone v Goff* (1975) 53 CA3d 191, 127 CR 390; 4 Witkin, Summary of California Law, *Security Transactions in Real Property* §§182-184, 187 (10th ed 2005); California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 5 (4th ed Cal CEB 2009).

Although a lender may obtain its own policy covering its separate insurable interest in the property, a single policy is usually written covering the owner and containing a clause in favor of the lender. In this way, the interests of both parties are protected under one policy at a lower cost, because no additional charge is made for the lender's coverage. Lenders customarily require the borrower to insure the property as a condition of the loan, and failure to maintain the insurance in force places the borrower in default under the deed of trust. Most deeds of trust provide that insurance proceeds either be used to repair the property or be applied to the unpaid loan balance, at the lender's option. See *JEM Enters. v Washington Mut. Bank* (2002) 99 CA4th 638, 121 CR2d 458.

In *Schoolcraft v Ross* (1978) 81 CA3d 75, 146 CR 57, the court held that the lender must exercise its option in good faith, and, to the extent the security has not been impaired, the proceeds must be used to repair the property. Civil Code §2924.7(b) and Fin C §1227.3 allow a lender to enforce its rights under a deed of trust to control the insurance proceeds following a casualty, but they are expressly subject to the borrower's right ultimately to obtain disbursement of the proceeds for restoration to the extent required by *Schoolcraft v Ross, supra*.

© The Regents of the University of California

§13.27 B. Loss Payable Clauses

A mortgagee or other lienholder has no right to the insurance benefits unless named as an additional insured or as a "loss payee." *Foothill Village Homeowners Ass'n v Bishop* (1999) 68 CA4th 1364, 1373, 81 CR2d 195. There are two general types of loss payable clauses: the simple loss payable clause (see §13.28) and the standard loss payable clause (see §13.29).

© The Regents of the University of California

§13.28 1. Simple Loss Payable Clause

A "simple" or "open" loss payable clause directs the insurer to pay the proceeds to the lienholder "as its interests may appear" before the insured receives payment under the policy. Under the simple loss payable clause, the lienholder is simply an appointee to receive the insurance proceeds to the extent of its interest, and its right of recovery is no greater than the right of the insured. Under the simple loss payable clause (*Home Sav. v Continental Ins. Co.* (2001) 87 CA4th 835, 841, 104 CR2d 790):

- No separate contract exists between the insurer and lienholder;
- The lienholder pays no consideration; and
- The lienholder's claim is subject to any defenses that the insurer could raise against the insured, *i.e.,* the insured's breach of conditions may bar the lienholder's claim.

© The Regents of the University of California

§13.29 2. Standard Loss Payable Clause

A typical "standard" or "union" or "New York" loss payable clause, such as that in the ISO Homeowners 3 Special Form (HO 00 03 10 90), provides:

> If a mortgagee is named in the policy, any loss payable… will be paid to the mortgagee and you, as interests appear….
>
> If we deny your claim, that denial will not apply to a valid claim of the mortgagee, if the mortgagee: (a) Notifies us of any change in ownership, occupancy or substantial change in risk of which the mortgagee is aware; (b) Pays any premium due under this policy on demand if you have neglected to pay the premium; (c) Submits a signed, sworn statement of loss within 60 days after receiving notice from us of your failure to do so.

Although the language of standard loss payable clauses may differ, the hallmarks of such a clause are provisions requiring notice to the mortgagee before cancellation and payment of premiums by the mortgagee on demand. *Home Sav. v Continental Ins. Co.* (2001) 87 CA4th 835, 848, 104 CR2d 790. In case of doubt, a loss payable clause calling for payment of proceeds is construed to be a standard loss payable clause. Under a standard loss payable clause (*Home Sav. v Continental Ins. Co., supra*):

- A separate contract is deemed to exist between the insurer and the lienholder;
- The lienholder's promise to pay premiums if the insured fails to do so is the consideration for the separate contract; and
- The lienholder's claim is not subject to any defenses the insurer might raise against the insured.

Thus, an insured's arson or other intentional destruction of the insured property will not defeat the claim of an innocent lienholder. 87 CA4th at 849.

© The Regents of the University of California

§13.30 C. Effect of Insured's Fraud

When one insured commits arson or fraud, an issue may arise regarding coverage for a coinsured's claim. In the past, insurers have argued that if property is held jointly, and one insured was guilty of arson or other fraud, all other coinsureds will be subject to the same defenses. The answer to this question appears to depend on the language of the policy.

The California Standard Form Fire Insurance Policy found in Ins C §2071 precludes coverage if the insured has willfully concealed or misrepresented any material fact or circumstance concerning the insurance or the subject of it, or the interest of the insured in it, or in case of any fraud or false swearing by the insured relating to it. In *Watts v Farmers Ins. Exch.* (2002) 98 CA4th 1246, 120 CR2d 694, the court held that, because the language adopted by the legislature does not specifically state that the act of any insured will be attributed to all insureds, the intent is that coverage be severable and that an innocent coinsured be able to recover for his or her proportionate share of the damaged property. 98 CA4th at 1260. Thus, when a policy precludes recovery as a result of fraud on the part of "the insured," the recovery is precluded only for the insured who committed the fraud, and the innocent coinsured is allowed to recover. 98 CA4th at 1261. However, when a policy precludes recovery as a result of fraud on the part of "any insured," the effect of one insured's fraudulent acts precludes recovery for all insureds, and an innocent coinsured is thus precluded from recovery. 98 CA4th at 1258.

© The Regents of the University of California

D. Credit Bids and Full Credit Bids

§13.31 1. Full Credit Bid Rule

In a nonjudicial foreclosure or trustee sale, the lender may make a "full credit bid," which is an amount equal to the unpaid principal and interest of the debt being foreclosed on, plus the costs, fees, and other expenses of foreclosure. If the lender buys the property through a full credit bid, the lien on the property is extinguished and the lender may not collect any damages for waste from the debtor or the debtor's successors even if the market value of the property is actually less than the amount of the bid. *Cornelison v Kornbluth* (1975) 15 C3d 590, 606, 125 CR 557. A full credit bid, in essence, fixes the value of the property between the lender and the borrower. Such a bid also prevents a foreclosing lender from collecting property insurance proceeds for damage to the property that occurred before purchase. The lender's only interest in the property is the repayment of the debt. The lender's interest having been satisfied, any other payment would result in a double recovery. *Track Mortgage Group, Inc. v Crusader Ins. Co.* (2002) 98 CA4th 857, 864, 120 CR2d 228; *Alliance Mortgage Co. v Rothwell* (1995) 10 C4th 1226, 1238, 44 CR2d 352. On the credit bid rule in general, see §13.32; California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 2 (4th ed Cal CEB 2009).

© The Regents of the University of California

§13.32 2. Credit Bid Rule

In the case of an insurer's bad faith failure to pay a foreclosing lender's claim for prepurchase damage to insured property, if the lender purchases the property for less than a full credit bid, the lender's contract damages are limited to the difference between the amount secured by the deed of trust and the lender's credit bid at the foreclosure sale. This is referred to as the "credit bid rule." *Track Mortgage Group, Inc. v Crusader Ins. Co.* (2002) 98 CA4th 857, 866, 120 CR2d 228. The *Track Mortgage* court further held that the lender's tort damages for bad faith are also limited by the credit bid rule absent a showing that the insurer's conduct caused the lender to make the credit bid. In other words, unless the insurer's conduct caused the lender's bid to be higher than the actual value of the property, the lender's damages will be reduced by its credit bid. On the full credit bid rule in general, see California Mortgages, Deeds of Trust, and Foreclosure Litigation, chap 2 (4th ed Cal CEB 2009).

© The Regents of the University of California

V. COMMON TYPES OF PROPERTY INSURANCE

§13.33 A. Noncommercial Property

There are too many different types of policies to discuss them all in this chapter. The Insurance Services Office (ISO) issues standard forms of policies that are used by many insurers. For information about the ISO, see the ISO website listed in the Directory. This chapter refers to ISO forms for typical language and form designations and numbers. The letters at the beginning of the ISO designation refer to the respective policy type, such as "CP" for commercial property, "BP" for business property, "FP" for farm property, and so on. The last two sets of digits indicate the month and year the form was first released for use, *i.e.,* "10 01" refers to October 2001. This is a convenient way to determine whether a policy contains the most recent policy forms. A typical policy will contain one or more basic forms, plus additional forms for declarations, conditions, optional coverages, and exclusions.

Often insurers draft their own forms, using parts of the ISO policy language and revising other parts. Insurers' policy forms use different designations and numbers.

PRACTICE TIP: Practitioners should not assume that all forms are the same, or even similar. In each transaction, the insurance policy should be reviewed carefully to determine which risks are covered and which are not. Although this lack of uniformity makes it difficult to draft contract provisions specifically, because not all insurers will use the same policy form designation and number, the difference in policies means some policies may afford broader coverage. Moreover, caution should be used in referring to specific policy forms in real estate contracts, because that may limit the pool of insurers that can provide the coverage. In addition, reference to specific policy forms may create problems if a form is changed or a specific edition is no longer available.

© The Regents of the University of California

§13.34 1. Fire

Insurance Code §2071 adopted the California Standard Form Fire Insurance Policy. The only losses covered by this policy are fire, lightning, and losses caused by removal of property from the premises when endangered by fire or lightning. Coverage is limited to the "actual cash value of the property at the time of loss," not exceeding the cost to repair or replace the property with material of like kind and quality, and without any allowance for increased cost of repair or reconstruction arising from any ordinance or law. No coverage is afforded for business interruption, extra expense, or rental value.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.35 2. Homeowners

§13.35 2. Homeowners

As in the building and personal property coverage forms (see §13.38), there are three principal variations of the homeowner's coverage forms offered by the ISO: Contents Broad Form (HO 00 04 10 90); Broad Form (HO 00 02 10 90); and Special Form (HO 00 03 10 90). In each form, the property coverages are divided into parts:

- Coverage A—Dwelling;
- Coverage B—Other Structures;
- Coverage C—Personal Property; and
- Coverage D—Loss of Use.

Coverage may also be available for:

- Debris removal;
- Reasonable repairs;
- Trees, shrubs, and other plants;
- Fire Department service charge;
- Property removed;
- Credit card, forgery, and counterfeit money;
- Loss assessment;
- Collapse;
- Glass or safety glazing material;
- Landlord's furnishings;
- Ordinance or law; and
- Grave markers.

The Contents Broad Form (often called the HO-4) affords coverage for contents for the same perils as covered in the Broad Form (see below), but does not afford coverage for the dwelling or other structures.

The Broad Form (often called the HO-2) covers fire or lightning, windstorm or hail, theft, explosion, smoke, damage from vehicles and aircraft, glass breakage, removal of property endangered by peril, vandalism and malicious mischief, and riot or civil commotion. The HO-2 also covers building collapse; freezing of or accidental discharge of water or steam from within plumbing, heating, or air-conditioning systems and domestic appliances; falling objects; weight of ice, snow, or sleet; and rupture or bursting of steam or hot water heating systems.

The Special Form (often called the HO-3) provides comprehensive coverage for "all risks" except certain named perils, such as earthquake and flood, and provides coverage for damage to personal property caused by any of the perils covered by the HO-2. For an additional premium, a special personal property coverage endorsement can usually be added to extend the HO-3 to provide "all-risks" coverage on unscheduled personal property.

Homeowners—Perils Insured Against

Perils	*Forms Providing Coverage**
Fire or Lightning	All Forms
Windstorm or Hail, Explosion, Riot or Civil Commotion, Aircraft, Vehicles, Smoke, Volcanic Eruption	All Forms
Vandalism or Malicious Mischief	All Forms
Theft	All Forms
Volcanic eruption	All Forms
Falling objects; Weight of ice, snow or sleet; Accidental discharge of water or steam; Sudden and accidental tearing apart of a	All Forms

heating system or appliance; Freezing; Sudden accidental damage from artificial electric current	
Additional risks with certain exceptions (Special Coverage)	Only HO-3 (A, B, D) and HO-5 (A, B, C, D)

*HO-2 (Broad Form); HO-3 (Special Form); HO-4 (Contents Broad Form); HO-6 (Unit Owners Form); HO-5 (Comprehensive); HO-8 (Modified Coverage)

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.36 3. Dwellings

§13.36 3. Dwellings

A dwelling policy provides more limited coverage than a homeowner's policy. A dwelling policy provides property coverage only, while a homeowner's policy offers a combination of property and liability coverages. Like homeowner policies, dwelling policies are divided into parts:

- Coverage A—Dwelling;
- Coverage B—Other Structures;
- Coverage C—Personal Property;
- Coverage D—Fair Rental Value; and
- Coverage E—Additional Living Expense.

Coverage may also be available for:

- Debris removal;
- Improvements, additions, and alterations;
- World-Wide coverage;
- Reasonable repairs;
- Property removed;
- Trees, shrubs, and other plants;
- Fire Department service charge;
- Collapse;
- Glass or safety glazing material; and
- Ordinance or law.

As with homeowners' policies (see §13.35), insureds may choose a form offering "Broad" coverage (DP 00 02 12 02, often called the DP2 policy), or a form offering "Special" coverage (DP 00 03 12 02, often called the DP3 policy). Dwelling policies may be used to insure homes that do not qualify for homeowners' insurance. For example, dwelling policies are commonly used to insure seasonal homes that are unoccupied for portions of the year. To qualify for dwelling insurance, a building does not have to be occupied by the owner, and it may even be under construction. Some types of stationary mobilehomes qualify, as well as homes with up to five boarders and four-unit apartment complexes. (Although some mobilehomes may qualify for the broader coverage of a homeowners' policy.)

Dwelling Property—Perils Insured Against

Perils	*Forms Providing Coverage**
Fire or Lightning; Internal Explosion	All Forms
Extended Coverage, meaning Windstorm or Hail; Explosion; Riot or Civil Commotion; Aircraft; Vehicles; Smoke; Volcanic Eruption	DP 00 02; DP 00 03; Optional with DP 00 01 (may only be written for the perils of Fire or Lighting, Internal Explosion)
Vandalism or Malicious Mischief	DP 00 02; DP 00 03; Optional with DP 00 01 (may only be written with Extended Coverage)
Damage by Burglars; Falling objects; Weight of ice, snow or sleet; Accidental discharge of water or steam; Sudden cracking of a steam or hot water heating system; Freezing; Sudden damage from	DP 00 02; DP 00 03

artificial electric current	
Additional risks with certain exceptions (Special Coverage)	DP 00 02; DP 00 03 provides only Coverages A and B

*DP 00 01(Dwelling Property 1 Basic Form);
DP 00 02 (Dwelling Property 2 Broad Form);
DP 00 03 (Dwelling Property 3 Special Form)

© The Regents of the University of California

§13.37 4. Condominium Owners

Because condominiums present unique issues regarding common walls or common areas, specialized policies have been developed for them, such as the ISO Unit Owners Form (HO 00 06 05 01). This policy covers alterations, appliances, fixtures, and improvements that are contained within the "residence premises," and personal property.

Covenants, conditions, and restrictions (CC&Rs) may divide responsibility for maintaining insurance between the homeowners association and the individual unit owners. This can complicate the analysis of the coverage available for a loss, and may require the court to examine both the policy and the CC&Rs.

For example, in *Palacin v Allstate Ins. Co.* (2004) 119 CA4th 855, 14 CR3d 731, the CC&Rs required the homeowners association to obtain a master "blanket" property insurance policy for the development, including the external and internal structure of the condominium units, naming each unit owner as an insured. The CC&Rs stated that no owner could separately insure his or her unit or any part of it against loss by fire or other casualty, with two exceptions. First, owners could insure their personal property against loss. Second, any improvements made by unit owners within their unit could be separately insured by the owner, but the insurance had to be limited to the type and nature of coverage commonly known as tenant improvements. 119 CA4th at 863. These provisions were intended to avoid double coverage. 119 CA4th at 864. The unit owner purchased a "Condominium Owners" policy that provided coverage for the following (119 CA4th at 859):

> items of real property pertaining directly to your residence premises *which are your insurance responsibility as expressed or implied under the governing rules of the condominium*. This includes fixtures, construction materials and supplies, installations or additions comprising a part of the residence premises, only when situated within that portion of the premises used exclusively by you and made or acquired at your expense.

The unit owners made a claim for water damage to the interior of their unit caused by a water leak from a neighboring unit. The insurer denied coverage, contending that the homeowners association was responsible for obtaining insurance for such a loss, and that the unit owner's policy did not cover the loss. The court noted that it had to engage in a double-layered analysis, examining both the CC&Rs and the policy that incorporated the CC&Rs. 119 CA4th at 864. The court held that the provision in the CC&Rs permitting the unit owner to obtain separate insurance constituted "implied responsibility" to obtain insurance, if the unit owner elected to do so. 119 CA4th at 865. The court also held that paint and carpet pad (and carpet) could constitute "tenant improvements." 119 CA4th at 867.

© The Regents of the University of California

B. Commercial Property

§13.38 1. Building and Personal Property

The ISO Building and Personal Property Coverage Form (CP 00 10 04 02) is a commonly used form. See §13.100. This form does not identify the covered causes of loss; rather the insured must decide which losses will be covered by electing to purchase one of the following:

- Basic Form (CP 10 10 04 02), which covers fire, lightning, explosion, windstorm or hail, smoke, aircraft or vehicles, riot or civil commotion, vandalism, sprinkler leakage, sinkhole collapse, and volcanic action;
- Broad Form (CP 10 20 04 02), which covers the causes of loss in the Basic Form, plus falling objects; weight of snow, ice or sleet; and water damage;
- Special Form (CP 10 30 04 02), which covers all risks of direct physical loss that are not excluded or limited by the policy.

© The Regents of the University of California

§13.39 2. Businessowners Special Property

The ISO Businessowners Special Property Coverage Form is BP 00 02 12 99. Under this form, all risks of direct physical loss are covered, unless excluded or limited by the policy.

© The Regents of the University of California

§13.40 3. Boiler and Machinery

As the name implies, boiler and machinery coverage was originally developed for the risk of a steam boiler explosion when many businesses generated power for machinery and equipment by using steam boilers. As currently used, this coverage may more accurately be thought of as equipment breakdown coverage. A typical form is the ISO Boiler and Machinery Coverage Form (BM 00 25 06 95). Coverage is afforded for costs of repairing or replacing the equipment, loss of income or extra expense incurred during repairs, and damage to other people's property in the care, custody, and control of the insured. In addition, refrigeration interruption coverage may be included.

© The Regents of the University of California

§13.41 4. Theft, Disappearance, and Dishonesty

Theft, disappearance, and dishonesty coverage applies to theft, disappearance, or destruction of "money" and "securities" that are typically excluded in other coverages. Coverage may be afforded for loss while money or securities are in the custody of an armored car company. Losses due to employee dishonesty are not covered. The current edition of the ISO form is CR 00 04 10 90.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.42 5. Robbery and Safe Burglary

§13.42 5. Robbery and Safe Burglary

The current edition of the ISO Robbery and Safe Burglary Coverage Form is CR 00 05 10 90. This coverage typically excludes loss of money or securities. Safe burglary coverage typically requires that the safe be locked and there be visible marks of forced entry of the safe. Losses due to employee dishonesty are not covered.

© The Regents of the University of California

§13.43 6. Premises Burglary

The current edition of the ISO Premises Burglary Coverage Form (CR 00 06 10 90) excludes loss of money or securities. The burglary coverage typically requires evidence of forcible entry or exit. The robbery coverage is typically limited to robbery of a watchperson, *i.e.,* someone who has no duties other than having care and custody of the property inside the premises. Losses due to employee dishonesty are not covered.

© The Regents of the University of California

§13.44 C. Builders' Risk

Builders' risk policies indemnify for loss of or damage to a building under construction. They are normally written for a specified dollar amount on the building and apply only during the course of construction. The coverage customarily includes fire, extended coverage, and vandalism and malicious mischief. Builders' risk coverage can be extended to a "special" form as well. The builders' risk policy also may include coverage for items in transit to the construction site (up to a certain percentage of value) and items stored at the site. For further discussion of builders' risk insurance, see California Construction Contracts, Defects, and Litigation, chap 10 (Cal CEB 2008).

© The Regents of the University of California

§13.45 D. Pollution

From 1973 to 1986, most Comprehensive General Liability policies (now referred to as Commercial General Liability (CGL) policies) excluded losses caused by pollution unless the release, dispersal, or discharge was "sudden and accidental." In 1986, virtually all CGL policies were amended to add an "absolute pollution exclusion" to eliminate coverage for pollution losses no matter how they were caused. See discussion of the "qualified pollution exclusion" and the "absolute pollution exclusion" in *McKinnon v Truck Ins. Exch.* (2003) 31 C4th 635, 644, 3 CR3d 228.

As a result, a new market emerged for liability insurance for pollution-related losses. There are now many different types of policies, for both first party and third party risks. However, there are no standardized forms for these types of policies, which makes discussion of specific coverages and exclusions difficult. The common types of provisions in these kinds of policies are discussed in §§13.46-13.51. For further discussion of hazardous waste, see chap 7.

NOTE: In *McKinnon,* the supreme court's interpretation of the term "pollutant" applied to an exclusion, which required that the term be interpreted narrowly. The terms "pollutant" or "pollution conditions" in the policies discussed in §§13.46-13.51 appear in the insuring language, which requires a broad interpretation to afford the greatest possible protection to the insured. *McKinnon,* 31 C4th at 648. It remains to be seen how broadly courts will interpret the terms "pollutant" or "pollution conditions" in these types of policies, and whether they will be applied to any liabilities other than "conventional environmental pollution." For a further discussion of *McKinnon*, see §13.86.

© The Regents of the University of California

§13.46 1. Pollution Legal Liability

Generally, Pollution Legal Liability (PLL) policies provide coverage for on-site cleanup of the insured premises triggered by first party discovery, as well as third party claims for bodily injury, property damage, and cleanup costs (both on-site and off-site). Both coverages apply to "pollution conditions," which may be defined as the discharge, dispersal, release, or escape of any solid, liquid, gaseous, or thermal irritant or contaminant, including, but not limited to, smoke, vapors, soot, fumes, acids, alkalis, toxic chemicals, medical waste, and waste materials into or upon land, or any structure on land, the atmosphere, or any watercourse or body of water, including groundwater, provided such conditions are not naturally present in the environment in the amounts or concentrations discovered.

Even after selling a property, the former owner may still face liability for cleanup costs. See §§7.11-7.12. PLL policies provide coverage for unknown pollution at covered locations specified in the policy and may cover off-site pollution resulting from conditions on the insured location. Costs of current cleanup efforts and costs related to known contamination are not covered. PLL policies usually cover liability for bodily injury, property damage, and cleanup costs. They may also include business interruption coverage.

© The Regents of the University of California

§13.47 2. Elements of Liability Defined

Because there are no standardized pollution policies, there may be a disparity in how different carriers define similar terms, and as a result, the scope of coverage afforded may differ. However, the coverages afforded by a Pollution Legal Liability policy generally include the following:

Cleanup costs. This generally refers to reasonable and necessary expenses for the investigation, removal, remediation, monitoring, or disposal of soil, surface water, groundwater, or other contamination. Such costs must be either required by environmental laws or actually incurred by a governmental entity. Carriers may require that no such expenses be incurred by the insured without the insurer's written consent, which may not be unreasonably withheld or delayed.

Restoration costs. These may be included as part of cleanup costs. Restoration costs refer to costs incurred to repair, replace, or restore real or personal property damaged during cleanup operations. Such costs may be limited to no more than the present value of the property before cleanup operations.

Natural resource damage. This may include physical injury to or destruction of land, fish, wildlife, biota, air, water, groundwater, drinking water supplies, and other similar resources belonging to, managed, or controlled by a governmental entity or Indian tribe. Natural resource damage may also include loss of the value of such resources.

Property damage and bodily injury. These may be defined similarly to the same terms used in commercial general liability policies (see §13.45). Property damage may be defined as physical injury to or destruction of tangible property of others, and may include the loss of use and diminution in value of such property. In addition, property damage may include loss of use of, but not diminution in value of, tangible property of parties other than the insured that has not been physically injured or destroyed. Bodily injury may be defined as physical injury, sickness, disease, mental anguish or emotional distress, or death resulting from any of these.

Typically, defense costs will be included in the definition of "loss," so that defense costs will be applied against any deductible and will also reduce any applicable policy limit.

© The Regents of the University of California

§13.48 3. Exclusions From Liability

Pollution legal liability coverage is usually written on a claims-made basis. This means the coverage applies to loss arising before the inception of the policy, as long as the claim is made during the policy period. As a result, the insurance application will require the prospective insured to verify that there are no known pollution conditions at the premises. The policy will also undoubtedly contain exclusions for the following pollution conditions:

- Those caused by the insured's intentional conduct;
- Those caused by the insured's willful or deliberate noncompliance with any statute, regulation, ordinance, administrative complaint, notice of violation, notice letter, executive order, or instruction of any governmental agency or body; and
- Those arising from pollution conditions existing before the inception date and known by a responsible insured and not disclosed in the application.

© The Regents of the University of California

§13.49 4. Cleanup Cost Cap

Cleanup cost cap (CCC) coverage is a first party coverage designed to protect against the risk entailed in beginning or continuing an environmental remediation project at a specific location. It covers cost overruns when the remediation project exceeds the anticipated costs of the remediation plan. The coverage may include both known pollutants and unknown pollutants discovered during the cleanup operation. The details of a remedial plan and the anticipated costs of the remediation must be set forth in an endorsement defining the remedial plan.

EXAMPLE: If the remedial action plan indicates the site can be cleaned up for $1 million, and the policy has a $100,000 deductible with a $5 million limit, the policy would apply to cost overruns between $1.1 million (the estimated cost plus the $100,000 deductible) and the $5 million policy limit.

These policies commonly exclude costs of legal defense, negotiations with governmental agencies, regulatory fines and penalties, radioactive contamination, asbestos contamination, and contractual liability. See *Certain Underwriters at Lloyd's of London v Superior Court* (2001) 24 C4th 945, 103 CR2d 672 (in standard commercial general liability policy, insurer had no duty to indemnify insured for environmental cleanup costs ordered by administrative agency, because such costs are not damages); see also *County of San Diego v Ace Prop. & Cas. Ins. Co.* (2005) 37 C4th 406, 33 CR3d 583 (in nonstandard third party liability insurance policy, expenses incurred by county (1) incident to agency cleanup order for environmental contamination and (2) in settling related third party property damage claims arising from contamination were not covered by policy). However, the insuring language of the policy in *Powerine Oil Co., Inc. v Superior Court* (2005) 37 C4th 377, 382, 33 CR3d 562, extended the insurer's indemnification obligation to administratively imposed environmental response costs.

Cleanup costs are generally defined as reasonable and necessary costs and expenses incurred solely for cleanup. Cleanup costs generally do not include legal expenses or costs; nor do they include costs or expenses incurred in preparing the remedial plan, but may include costs or expenses incurred in preparing a supplementary remedial plan to address previously unknown pollutants discovered during the remediation. The policy usually excludes any cleanup costs arising from or connected with the following:

- Bodily injury or property damage or third party liability to any party for any reason;
- The insured's intentional, willful, or deliberate noncompliance with any statute, regulation, ordinance, administrative complaint, notice of violation, notice letter, executive order, instruction of any governmental agency or body, or any criminal acts of any insured; or
- Pollutants that existed before the inception date and known by any manager or supervisor responsible for environmental affairs or any officer, director, or partner of the named insured and that were not disclosed in the application.

The coverage generally applies in excess of a self-insured retention or deductible, which is generally the amount of the expected cost of cleanup as specified in the remedial plan, plus an additional buffer amount, often called a coinsurance participation, which is a percentage of the anticipated cleanup costs.

© The Regents of the University of California

§13.50 5. Property Transfer

Property transfer policies are specifically tailored for real estate transactions. These policies usually provide coverage for pollution legal liability (PLL) (see §13.46) and cleanup cost cap (see §13.49). Like PLL policies, property transfer policies provide coverage for preexisting, unknown contamination. Some may also provide coverage for known contamination below reportable levels, or even levels above regulatory limits but permitted by a governmental agency.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.51 6. Secured Lender or Secured Creditor

§13.51 6. Secured Lender or Secured Creditor

Secured creditor coverage provides first party coverage and pays the outstanding loan balance when a default occurs and an environmental condition exists at the location. Some policies pay either the outstanding loan balance or cleanup costs, whichever is less. In addition, these policies may also provide third party coverage and protect the lender from claims for bodily injury, property damage, and cleanup costs. Further, the policy may afford coverage for the lender for cleanup costs incurred by the lender after foreclosure.

The default and pollution conditions coverage may state:

> The Company will indemnify the Insured for Loss, if during the Policy Period and prior to Foreclosure, there is a Default by a Borrower on a Commercial Real Estate Loan secured by an Insured Property, Leasehold or Fixed Assets, and there are Pollution Conditions on, under or emanating from the same Insured Property prior to or while the Commercial Real Estate Loan is in default.

The coverage for third party claims may state:

> The Company agrees to pay Loss on behalf of the Insured that the Insured becomes legally obligated to pay as a result of Claims first made against the Insured and reported to the Company, in writing, during the Policy Period, for Bodily Injury, Property Damage or Cleanup Costs resulting from Pollution Conditions on, under or emanating from an Insured Property.

The coverage for cleanup of pollution conditions may state:

> The Company agrees to pay Loss on behalf of an Insured, after Foreclosure, if Cleanup Costs are sustained because there are Pollution Conditions on, under or emanating from the Insured Property during the Policy Period provided that where required, such Pollution Conditions have been reported by the Insured to the appropriate governmental agency in compliance with applicable Environmental Laws, in effect on the date of discovery.

Loss may be defined differently for each type of coverage. For default and pollution conditions, "loss" may be defined as the outstanding balance on the date of default, including principal and accrued interest. For the third party claims coverage, "loss" may be defined as monetary awards or settlements of compensatory damages for bodily injury, property damage, or cleanup costs, and costs and expenses incurred in the defense, investigation, and adjustment of such claims. With respect to cleanup cost coverage, "loss" may be defined as "cleanup costs."

All three coverages will likely exclude coverage for any loss:

- Arising from pollution conditions resulting from or attributable to the insured's intentional, willful, or deliberate noncompliance with any statute, regulation, ordinance, administrative complaint, notice of violation, notice letter, executive order, or instruction of any governmental agency or body;
- Arising from pollution conditions resulting from an intentionally illegal act or omission of the insured, if the insured knew that the pollution conditions would result; or
- Arising from pollution conditions existing before the effective date of coverage for an insured property, and not otherwise specifically excluded by endorsement to the policy, if as of such date the insured knew that such pollution conditions could give rise to a loss under the policy and failed to disclose those pollution conditions to the insurer, or the insurer did not otherwise learn of the pollution conditions from engineering reports, environmental spreadsheets, the secured creditor impaired-property questionnaire, or from other technical reports the insurer obtains independently.

© The Regents of the University of California

§13.52 E. Earthquake Coverage

In 1994, the Northridge earthquake, registering 6.7 on the Richter scale, caused $12.5 billion in damage to residential property. As a result, many insurers severely restricted or refused to write new homeowners' policies because of the state mandate that they offer earthquake insurance. In response, in 1996, the legislature established the California Earthquake Authority (CEA). See Ins C §§10089.5-10089.54. The CEA is a privately financed, publicly managed entity that issues policies through participating insurers. The CEA is now the world's largest residential earthquake insurer. The CEA website (listed in the Directory) has a program to calculate the estimated annual earthquake premium. Californians can also buy earthquake policies outside the CEA.

The CEA sells earthquake policies to homeowners, mobilehome owners, condominium owners, and renters. The Base Limits Policy offers structure coverage equal to the structure coverage limit of the homeowners' or mobilehome owners' policy. The structure policy limit for the condominium owners' policy is $25,000 to repair or replace structural components of the condominium for which the owner is legally responsible. There is no structure coverage under the Renters policy. Each Base Limit policy offers a $5000 limit for contents coverage and a $1500 limit for the insured's additional living expenses if the premises are uninhabitable after an earthquake. The homeowners', mobilehome owners', and condominium owners' Base Limits Policies provide up to $10,000 for additional costs of repair incurred solely to comply with local residential building codes in effect on the date of the damaging earthquake. The homeowners', mobilehome owners', and condominium owners' Base Limits Policies are subject to a deductible of 15 percent of the structure coverage limit. Only losses to the structure count toward meeting this deductible. The condominium owners' policy also offers a limit of $25,000 to $50,000, depending on the market value of the unit, for loss assessments imposed by a homeowners association.

Coverage for earthquake damage to commercial property may be difficult to obtain. Such coverage may be afforded through a stand-alone policy, or by endorsements adding earthquake as a covered cause of loss.

© The Regents of the University of California

§13.53 F. Flood Insurance

In 1968, because of the rising cost of taxpayer-funded disaster relief for flood victims, Congress created the National Flood Insurance Program (NFIP), enacted by the National Flood Insurance Act (42 USC §§4001-4129). Policies are issued by private insurers participating in the NFIP. The NFIP offers three standard flood insurance policy (SFIP) forms (44 CFR pt 61, App A):

- Dwelling Policy Form (44 CFR pt 61, App A(1)), used to insure the structure and contents of single-family structures, one-to-four-family structures, townhouse or rowhouse structures, condominium units, manufactured or mobilehomes, residential cooperatives, and timeshares. See *Pecarovich v Allstate Ins. Co.* (9th Cir 2002) 309 F3d 652 (holding for homeowner by narrowly construing NFIP policy provision that excluded flood coverage when flood was confined to homeowner's premises).
- General Property Policy Form (44 CFR pt 61, App A(2)), used to insure other residential and nonresidential structures and their contents.
- Residential Condominium Building Association Policy Form (44 CFR pt 61, App A(3)), used for residential condominium building associations to cover the entire building under one policy, as well as improvements and personal property owned in common. It does not provide coverage for personal property owned exclusively by a unit owner.

All flood claim benefits paid under the NFIP are U.S. Treasury funds. *Van Holt v Liberty Mut. Ins. Co.* (3rd Cir 1998) 163 F3d 161, 165. Although "Write Your Own" carriers issue the insurance policies and process claims, they do so as fiscal agents of the United States. 42 USC §4071(a). The terms of the standard flood insurance program policies are set by the Federal Emergency Management Agency (FEMA), and carriers are not permitted to deviate from those terms. *Van Holt,* 163 F3d 161, 165. A suit against a carrier that issued a SFIP is essentially a suit against FEMA; *Flick v Liberty Mut. Fire Ins. Co.* (9th Cir 2000) 205 F3d 386, 393 n10. All claims under policies issued through the NFIP, including state law tort claims, must be brought in federal court. *McCormick v Travelers Ins. Co*. (2001) 86 CA4th 404, 103 CR2d 258. The statute that governs judicial review of SFIP claims does not grant the right to a jury trial. 42 USC §4072. In addition, extra-contractual claims asserted in SFIP disputes are preempted by federal law. *Pecarovich v Allstate Ins. Co.* (CD Cal 2003) 272 F Supp 2d 981, 987 (claims for bad faith, punitive damages, and interest preempted in SFIP dispute); *Scherz v S.C. Ins. Co.* (CD Cal 2000) 112 F Supp 2d 1000, 1007 (same); *Bianchi v State Farm Fire & Cas. Co.* (ND Cal 2000) 120 F Supp 2d 837-840 (dismissing bad faith claim and striking requests for emotional distress, punitive damages, and attorney fees).

© The Regents of the University of California

§13.54 G. Ancillary Coverages for Commercial Risks

In evaluating the overall worth of a business for purposes of sale or purchase, the building and fixtures may be only a fraction of the business's value. If a fire or other disaster causes the business to close, even for a short time, the loss of income, cost to replace computer equipment, cost to recover business records, possible loss of accounts receivables, and the expense of getting the business going again may be higher than the cost to restore the building.

© The Regents of the University of California

§13.55 1. Business Interruption Coverage

Coverage for business income and extra expenses (sometimes called "business interruption" coverage) applies to a necessary interruption of business that directly results from a covered loss. *Pacific Coast Eng'g Co. v St. Paul Fire & Marine Ins. Co.* (1970) 9 CA3d 270, 88 CR 122. Recovery may include lost profits, loss of earnings, and continuing expenses during the period of repair or restoration of property damaged or destroyed by reason of a covered peril (*Buxbaum v Aetna Life & Cas. Co.* (2002) 103 CA4th 434, 443, 126 CR2d 682) and is intended to return to the insured's business the amount of profit it would have earned had there been no interruption of the business. 103 CA4th at 443. However, items such as interest on loans, expenses resulting from delay in receiving final installment payments, late delivery damages, and overtime expenses in expediting completion and delivery of goods have been held to be indirect, consequential, or remote losses that do not constitute "business income." *Pacific Coast Eng'g Co.,* 9 CA3d at 273.

Moreover, business income insurance provides coverage only for losses resulting directly from interruption of the business, *i.e.,* operation of the plant, and not merely from interruption of work being done on the construction of a particular project at the time a covered loss occurred. *Pacific Coast Eng'g Co.,* 9 CA3d at 275.

Business income looks to the future and is not dependent on past profits. Coverage may be afforded on the basis of profit expectancies, although this will present proof problems. *General Ins. Co. v Pathfinder Petroleum Co.* (9th Cir 1944) 145 F2d 368, 369.

The ISO Business Income and Extra Expense Coverage Form (CP 00 30 04 02) provides coverage for "business income" and "extra expense." It may also provide optional coverage for "rental value" and "interruption of computer operations." The insuring language states:

> We will pay for the actual loss of Business Income you sustain due to the necessary "suspension" of your "operations" during the "period of restoration." The "suspension" must be caused by direct physical loss of or damage to property at premises which are described in the Declarations and for which a Business Income Limit of Insurance is shown in the Declarations. The loss or damage must be caused by or result from a Covered Cause of Loss. With respect to loss of or damage to personal property in the open or personal property in a vehicle, the described premises include the area within 100 feet of the site at which the described premises are located.

© The Regents of the University of California

§13.56 a. Covered Causes of Loss

In the same way as the property form (see §13.70), the ISO Business Income (and Extra Expense) Coverage Form (CP 00 30 04 02) requires the insured to select the risks that will be "covered causes of loss" by choosing a Covered Cause of Loss Form—Basic or Special. See discussion at §13.38.

© The Regents of the University of California

§13.57 b. Optional Coverage for Interruption of Computer Operations

The ISO Business Income (and Extra Expense) Coverage Form (CP 00 30 04 02) contains what is in effect an exclusion called an "additional limitation" that pertains to interruption of computer operations (Coverage A.4, "Additional Limitations—Interruption of Computer Operations," p 2). This limitation states that the coverage for business income does not apply to a suspension of operations caused by destruction or corruption of electronic data, or any loss or damage to electronic data, unless the insured purchases extended coverage for that risk.

This same form allows the insured to purchase additional coverage for this risk (Coverage A.5.d, "Interruption of Computer Operations"). If purchased, the additional coverage would apply to losses caused by a virus, harmful code, or similar instruction introduced into or enacted on a computer system (including electronic data) or a network to which it is connected, that is designed to damage or destroy any part of the system or disrupt its normal operation. The coverage does not apply to interruptions related to manipulation of a computer system (including electronic data) by any employee, including a temporary or leased employee, or by an entity retained by or for the insured to inspect, design, install, maintain, repair, or replace that system. The limit of coverage for interruption of computer operations is $2500 for all loss sustained or incurred in one policy year.

© The Regents of the University of California

§13.58 c. Described Premises

The insuring language of ISO Business Income (and Extra Expense) Coverage Form (CP 00 30 04 02) states that the suspension of operations must be caused by direct physical loss of or damage to property located at premises that are described in the declarations page of the policy and for which a business income limit of insurance is shown in the declarations. This precludes an insured with multiple business locations or even multiple businesses from attempting to insure them all without paying a separate premium for each. It also means that suspension of operations caused by a loss at another location will not be covered. For example, if a fire at a factory that is not a described premises causes the suspension of operations at the described premises because, *e.g.*, parts are not available, the loss will not be covered.

NOTE: Contingent business interruption coverage and contingent extra expense coverage is available from some insurers. It provides coverage for lost profits and extra expenses resulting from interruption of business at the premises of a customer or supplier. This coverage may be necessary if the insured depends on a single or a few suppliers or manufacturers for materials or merchandise, or one or a few customers to purchase the bulk of the insured's products, or a neighboring "anchor tenant" to attract customers.

© The Regents of the University of California

§13.59 d. Total Suspension Versus Partial Interruption

In the ISO Business Income (and Extra Expense) Coverage Form (CP 00 30 04 02) the term "suspension of operations" is defined as follows:

> a. The slowdown or cessation of your business activities; or
> b. That a part or all of the described premises is rendered untenantable, if coverage for Business Income including "Rental Value" or "Rental Value" applies.

Some cases have held that when the term "suspension" was not defined in the policy, a "suspension" required the complete cessation of business, and that a partial shutdown or slowdown would not constitute a "suspension" of operations. *Buxbaum v Aetna Life & Cas. Co.* (2002) 103 CA4th 434, 451, 126 CR2d 682; see also *Pacific Coast Eng'g Co. v St. Paul Fire & Marine Ins. Co.* (1970) 9 CA3d 270, 275, 88 CR 122. The definition in this ISO form defining "suspension" to include a "slowdown" should preclude such a result.

© The Regents of the University of California

§13.60 e. Period of Restoration

Generally, the period of restoration begins to run on the date of occurrence of a covered loss and ends on the date the property should be rebuilt, repaired, or replaced with reasonable speed and similar quality. Older policy forms stated that the insured must act with "due diligence and dispatch" to rebuild, repair, or replace. Notably, this may run beyond the date of policy expiration. See the ISO Business Income (and Extra Expense) Coverage Form (CP 00 30 04 02). If disputed, when the "period of restoration" ends may be a question of fact. See, *e.g., R&R Sails, Inc. v Insurance Co. of the State of Pennsylvania* (SD Cal 2009) 610 F Supp 2d 1222, 1230; See also *Shaw Mortgage Corp. v Peerless Ins. Co.* (SD Cal 2009) 615 F Supp 2d 1172 (period of restoration ended at earlier of (1) expiration of extended period provided by special endorsement after date of direct physical loss, or (2) when either property should have been repaired or rebuilt with reasonable speed and similar quality or when business was resumed at new permanent location, whichever came first).

NOTE: The insured in *Shaw Mortgage* could have purchased optional extended business income coverage, which would have provided business *income* coverage until the earlier of either the date that the store resumed its pre-loss level of business or 30 days after the store was repaired, rebuilt, or replaced. *Shaw Mortgage,* 615 F Supp 2d at 1175; ISO Business Income (and Extra Expense) Coverage Form CP 00 30 04 02.

© The Regents of the University of California

§13.61 f. Burden of Proof

If there are concurrent causes of loss, the insured has the burden of proof to establish the total amount of claimed loss resulting from covered causes. See *General Ins. Co. v Pathfinder Petroleum Co.* (9th Cir 1944) 145 F2d 368 (applying California law); Russ, 15A Couch on Insurance §57.32 (3d 1995). An insured claiming a business income loss for manufacturing typically must prove loss of sales, not just loss of production. The rationale for that requirement is that if no one wants to buy the product, reimbursing the insured for loss of production would put the insured in a better position than if no suspension had occurred, *i.e.,* the insured would have had to shut down the manufacturing plant because of lack of sales anyway.

© The Regents of the University of California

§13.62 g. Duty to Mitigate

The "period of restoration" ends when the insured could have rebuilt, repaired, or replaced the property with reasonable speed and similar quality. See §13.60. Some policies state that the insured must act with "due diligence and dispatch," which is a recognition of the general duty of an insured to mitigate damages when an insured loss occurs.

© The Regents of the University of California

§13.63 h. Extra Expense

Extra expense coverage is designed to reimburse the insured for reasonable amounts paid, over and above normal operating expenses, to return to normal operations as quickly as possible to help decrease the business income losses. The current edition of the ISO form (CP 00 30 04 02) combines business income coverage with extra expense coverage.

© The Regents of the University of California

§13.64 i. Rental Value

Rental value coverage protects against loss of rents that would have been earned from tenant occupancy of the premises, and fair rental value of any portion of the premises that would have been occupied by the insured. There is no separate ISO coverage form for rental value; this coverage is afforded as optional coverage under the Business Income (and Extra Expense) Coverage Form (CP 00 30 04 02). As with the business income coverage, (1) the loss of rental value must be caused by direct physical loss or damage at the described premises caused by or resulting from a covered cause of loss; and (2) rental value coverage applies for a limited time.

© The Regents of the University of California

2. Other Ancillary Coverages

§13.65 a. Computers and Electronic Equipment

Most property policies have specific limits for computers or other electronic equipment that will be insufficient for most businesses. The ISO has developed an Electronic Data Processing Coverage Form (AAIS IM 72 02 05 01), which permits the insured to select higher limits for various types of equipment, and certain types of data records and software programs. Unfortunately, no coverage is afforded for losses caused by computer viruses or hackers.

© The Regents of the University of California

§13.66 b. Computer Fraud

The proliferation of computers has increased the ways in which crime can occur. Computer fraud does not fall within the definition of "robbery" or "safe burglary" in a robbery and safe burglary policy, or within the definition of "burglary" in a premises burglary policy. The ISO has developed a specific form for computer fraud, CR 00 07 10 90. The coverage applies to "computer fraud," defined as

> theft of property following and directly related to the use of any computer to fraudulently cause a transfer of that property from inside the "premises" or "banking premises" to a person (other than a "messenger") outside those "premises" or to a place outside those "premises."

© The Regents of the University of California

§13.67 c. Valuable Papers

Valuable papers include proprietary information, books of account, deeds, manuscripts, abstracts, drawings, and card index systems; similar information may also be stored electronically. Most business property policies either exclude coverage for "valuable papers," or provide coverage at significantly reduced limits. For example, the ISO Building and Personal Property Coverage Form (CP 00 10 04 02) excludes coverage for "valuable papers" by listing them as "Property Not Covered." This form allows the insured to purchase extended coverage for valuable papers other than electronic data. The limit, shown on the declarations page of the policy, is $2500 unless the insured pays an additional premium for a higher limit.

Some companies offer separate coverages for valuable papers and records. The ISO Valuable Papers and Records Coverage Form (CM 00 67 05 01) defines "valuable papers and records" as follows:

> "Valuable papers and records" means inscribed, printed or written documents, manuscripts or records, including abstracts, books, deeds, drawings, films, maps or mortgages.
> But "Valuable papers and records" does not mean "money" or "securities," converted data, programs or instructions used in your data processing operations, including the materials on which the data is recorded.

Under this definition, it appears that data stored electronically would not be covered. The "Valuable Papers and Records" coverage is written on an "all-risk" basis. That is, all risks of direct physical loss not expressly excluded (such as fire, flood, etc.) are covered. The coverage contains several exclusions, however, including losses caused by or resulting from any dishonest or criminal act committed by the insured, or any partners, employees, directors, trustees, or authorized representatives of the insured, or anyone else to whom the property is entrusted for any purpose. Thus, if any records are lost, stolen, or vandalized by an employee, there will be no coverage for that loss.

© The Regents of the University of California

§13.68 d. Accounts Receivable

After a catastrophic loss, an insured may also lose records of accounts receivables. The inability to collect accounts receivable may create an even greater strain while the insured attempts to recover from the loss. The ISO Accounts Receivable Coverage Form (CM 00 66 09 04) affords coverage for (1) amounts due from customers that the insured is unable to collect; (2) interest charges on any loan required to offset amounts the insured is unable to collect pending payment of those amounts; (3) collection expenses in excess of normal collection expenses that are made necessary by the loss or damage; and (4) other reasonable expenses incurred to re-establish records of accounts receivable.

© The Regents of the University of California

VI. HOW DO PROPERTY COVERAGES WORK?

§13.69 A. "Covered Property" Versus "Property Not Covered"

Most property policies contain sections listing the property that is covered (often with a heading such as "Covered Property") and a separate section listing property that is not covered (often with the heading such as "Property Not Covered"). See, *e.g.*, ISO Building and Personal Property Coverage Form (CP 00 10 04 02) or ISO Homeowners 3 Special Form (HO 00 03 10 90).

Typically, covered property lists improvements at the identified location, including an identified structure, foundations, outbuildings, drives, walks, landscaping, and other improvements. Fixtures, personal property, business interruption, and loss of use may also be insured.

WARNING: Not all covered property is insured equally. Some policies limit coverage for outbuildings, drives, walks, detached garages, terraces, swimming pools, and similar structures. Serious underinsurance problems can result if attention is not paid to the monetary limits on the various types of property insured under the contract. This is also true for personal property and for business interruption or loss of use, which almost always occurs in a serious property loss.

In the past, a series of decisions held either that the term "dwelling" included the land on which the house sat, or that when earth movement is an insured peril, the insurer is liable for the cost of stabilizing the soil under the insured dwelling, up to the policy limit. See *Strickland v Federal Ins. Co.* (1988) 200 CA3d 792, 799, 246 CR 345 (earth movement was insured peril under homeowner's insurance policy; insurer liable for cost of stabilizing soil underlying insured's dwelling, up to policy limits); *Snapp v State Farm Fire & Cas. Co.* (1962) 206 CA2d 827, 833, 24 CR 44 (owners covered by and up to policy limit of $25,000, despite fact that landslide continued after expiration of policy); *Hughes v Potomac Ins. Co.* (1962) 199 CA2d 239, 248, 18 CR 650 (landslide caused loss of support essential to stability of insured's creekside home; measure of damages was market value loss to insured's home); *Pfeiffer v General Ins. Corp.* (ND Cal 1960) 185 F Supp 605, 608 (term "dwelling" included land underlying it). Under the "Property Not Covered" section of the Building and Personal Property Coverage Form (CP 00 10 04 02), however, "land (including land on which the property is located)" is not "covered property." Moreover, earth movement is now excluded as a covered peril under Exclusion B in all three ISO Causes of Loss forms (Basic Form (CP 10 10 04 02); Broad Form (CP 10 20 04 02); and Special Form (CP 10 30 04 02)). In *Fire Ins. Exch. v Superior Court* (2004) 116 CA4th 446, 454, 10 CR3d 617, the appellate court distinguished *Strickland* and *Snapp* and held that, because the policy specifically stated that land on which the dwelling is located was not covered, the court would give effect to the "clear and explicit" policy provision; the court rejected the argument that the term "dwelling" included the land underlying the structure.

© The Regents of the University of California

§13.70 B. Covered Causes of Loss

Commercial property and homeowners' policies are usually one of two types: (1) named risk (also known as "named perils" or "specified perils"), or (2) all risks (or "all perils"). Under a named-risk policy, such as the ISO Causes of Loss—Basic Form (CP 10 10 04 02), the coverage applies only to losses caused by "covered causes of loss" that are specifically listed in the policy.

For further discussion, see California Construction Contracts, Defects, and Litigation, chap 10 (Cal CEB 2008).

© The Regents of the University of California

§13.71 1. All Risks or All Perils

Under an all-risk policy, such as the ISO Causes of Loss—Special Form (CP 10 30 04 02), all risks of "direct physical loss" are covered unless they are specifically excluded. In other words, the scope of coverage is defined by the exclusions. *Julian v Hartford Underwriters Ins. Co.* (2005) 35 C4th 747, 751 n2, 27 CR3d 648; *Garvey v State Farm Fire & Cas. Co.* (1989) 48 C3d 395, 257 CR 292; *Freedman v State Farm Ins. Co.* (2009) 173 CA4th 957, 959 n1, 93 CR3d 296; *Fire Ins. Exch. v Superior Court* (2004) 116 CA4th 446, 464 n13, 10 CR3d 617. Under an all-risk policy, the insurer bears the burden of proving that the loss was caused by an excluded peril.

© The Regents of the University of California

§13.72 2. Named Risks or Named Perils

Under a named-risk or named-peril or named-peril policy, the initial focus is on whether the cause of loss is a named risk or named peril; only then do the exclusions become relevant. See *Garvey v State Farm Fire & Cas. Co.* (1989) 48 C3d 395, 406, 257 CR 292; see also *Freedman v State Farm Ins. Co.* (2009) 173 CA4th 957, 959 n1, 93 CR3d 296. The insured bears the burden of proving that the loss was caused by one (or more) of the specifically enumerated risks. See *Stubble v United Servs. Auto. Ass'n* (1973) 35 CA3d 498, 504, 110 CR 828.

NOTE: Some policies may afford "all risk" coverage for some types of property and "named risk" coverage for others. See, *e.g., Freedman*, 173 CA4th 957 at 959 (policy afforded "all risk" coverage for the insured dwelling, but "named risk" coverage for personal property).

© The Regents of the University of California

§13.73 C. Direct Physical Loss

Generally, insured property must suffer "direct physical loss" before an insurer will respond. Normally, a property policy insures against "fortuitous, active, physical forces such as lightning, wind, and explosion, which bring about the loss." Ins C §§22, 250; *Garvey v State Farm Fire & Cas. Co.* (1989) 48 C3d 395, 406, 257 CR 292; *Fire Ins. Exch. v Superior Court* (2004) 116 CA4th 446, 464 n13, 10 CR3d 617.

State Farm Fire & Cas. Co. v Superior Court (1989) 215 CA3d 1435, 1445, 264 CR 269, illustrates the limitations of the property contract. In *State Farm,* a condominium homeowners association alleged that building code violations, faulty workmanship, and fraud by the builder had sharply lowered the condominiums' value. In addition to repair costs, it sought coverage for "diminution in value" under its policy. The court of appeal held that diminution in value was not covered, because it did not involve direct physical loss to property: "The policy here states it insures against 'direct physical loss' except when due to certain enumerated causes; diminution of market value is not specifically excluded because it is not a 'cause' of loss; it is the measure of the loss caused by someone else." 215 CA3d at 1445.

In *Hughes v Potomac Ins. Co.* (1962) 199 CA2d 239, 18 CR 650, a covered peril caused a hillside to erode up to and beneath the footings of a building. However, there was no discernible direct physical loss to the structure. The court held that, if a rational person would not see fit to occupy the structure, that perception was enough to trigger a carrier's duty to respond. 199 CA2d at 248.

In *Western Fire Ins. Co. v First Presbyterian Church* (Colo 1968) 437 P2d 52, the court found "direct physical loss" to property where gasoline had entered the soil underneath a church. Gasoline vapors infiltrated the foundation, halls, and rooms, making the church unusable. The church had sought coverage for the expense of removing the gasoline vapors, but its carrier denied the claim. The Colorado Supreme Court found direct physical loss to property and coverage. 437 P2d at 55. Although the court recited the rule that the insured could not establish direct physical loss to property merely by alleging loss of use, the facts satisfied the court that there was physical injury or damage to the property. 437 P2d at 55.

In *Ward Gen. Ins. Servs., Inc. v Employers Fire Ins. Co.* (2003) 114 CA4th 548, 7 CR3d 844, however, a computer operator inadvertently hit the "delete" key, deleting the insured's database of client information. Although the insured incurred extra expenses in restoring its data and loss of business income because of the disruption, there was no mechanical or electrical failure, and no loss of or destruction of the storage medium on which the data had been maintained. The insured sought coverage for its extra expense and loss of income under the following forms: Business and Personal Property Coverage; Valuable Papers and Records Coverage; Electronic Equipment and Software Coverage; and Business Income Coverage (And Extra Expense). Each form required a "direct physical loss of or damage to" property. The appellate court held the adjectives "direct physical" modified both "loss of" and "damage to." 114 CA4th at 554. Further, the court held that the information itself, as information, was intangible. The court held that the loss of the database, with its consequent economic loss but with no loss of or damage to tangible property, was not a "direct physical loss of or damage to" covered property, and thus the loss was not covered under any of the forms. 114 CA4th at 556.

© The Regents of the University of California

§13.74 D. Exclusions

In most circumstances, an insurer is free to select the character of the risk it will assume, and it is liable only for a loss within the terms of the policy. *Fresno Economy Import Used Cars, Inc. v United States Fid. & Guar. Co.* (1977) 76 CA3d 272, 280, 142 CR 681. An insurer has the right to limit the coverage of a policy issued by it, and when it has done so, the plain language of the limitation must be respected. *Julian v Hartford Underwriters Ins. Co.* (2005) 35 C4th 747, 759, 27 CR3d 648; *Continental Cas. Co. v Phoenix Constr. Co.* (1956) 46 C2d 423, 296 P2d 801; *Fresno Economy Import Used Cars, Inc. v United States Fid. & Guar. Co., supra*. Words of an exclusion must be part of the working vocabulary of the average person, and must be phrased in a logical manner. *Blasiar, Inc. v Fireman's Fund Ins. Co.* (1999) 76 CA4th 748, 754, 90 CR2d 374. The insurer bears the burden to draft the exclusion in clear language comprehensible to a layperson. *Cal-Farm Ins. Co. v TAC Exterminators, Inc.* (1985) 172 CA3d 564, 578, 218 CR 407. Exclusionary clauses are subjected to heightened scrutiny by courts, and if the exclusion is not conspicuous, plain, and clear, it will be invalidated. *Thompson v Mercury Cas. Co.* (2000) 84 CA4th 90, 94, 100 CR2d 596.

Under settled rules for insurance policy interpretation, the court must accept a tenable construction of an exclusion most favorable to the insured. *Freedman v Queen Ins. Co.* (1961) 56 C2d 454, 15 CR 69.

See §13.84 for further discussion of exclusions.

© The Regents of the University of California

§13.75 1. Exceptions

Some exclusions contain exceptions that restore some of the coverage taken away by the exclusion. Thus, because an exception is somewhat analogous to insuring language, exceptions are construed broadly. *Old Republic Ins. Co. v Superior Court* (1998) 66 CA4th 128, 145, 77 CR2d 642, overruled on other grounds in *Vandenberg v Superior Court* (1999) 21 C4th 815, 841 n13, 88 CR2d 366. However, an exception to an exclusion cannot create coverage for a loss not otherwise covered under the insuring language. *Old Republic Ins. Co. v Superior Court, supra*.

© The Regents of the University of California

§13.76 2. Who Has the Burden of Proof?

The insurer has the burden of proof to establish the exclusion that bars coverage for the loss. *Garvey v State Farm Fire & Cas. Co.* (1989) 48 C3d 395, 405, 257 CR 292; *Roberts v Assurance Co. of Am.* (2008) 163 CA4th 1398, 1406, 78 CR3d 361 (insurer seeking summary judgment on ground claim is excluded has burden to prove claim falls within exclusion and once proven, burden shifts to insured to show existence of triable issue of material fact). Most cases place the burden of proof on the insured to establish that an exception to the exclusion applies. *Travelers Cas. & Sur. Co. v Superior Court* (1998) 63 CA4th 1440, 1454, 75 CR2d 54.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.77 E. When Does a Loss Occur?

§13.77 E. When Does a Loss Occur?

Property policies, like most insurance policies, are written to cover a specific period of time called the policy term or policy period. Whether the policy will cover damage that occurs before the inception of the policy period depends on whether the damage is episodic (see §13.78) or continuous (see §13.79).

© The Regents of the University of California

§13.78 1. Episodic Loss

Episodic loss or damage refers to damage that occurs at a specific point in time. For example, a fire, a tornado, or a fallen tree branch can be pinpointed to a specific date. Such damage must occur during the policy period for it to be covered under a property policy. See *Armstrong World Indus., Inc. v Aetna Cas. & Sur. Co.* (1996) 45 CA4th 1, 95, 52 CR2d 690 (releases of asbestos fibers occur sporadically, because of "episodic disturbances such as accidental striking, vandalism, water damage, and the like").

© The Regents of the University of California

§13.79 2. Continuous or Progressive Loss

Some types of losses or damage cannot be pinpointed to a specific date. For example, damage caused by a leaking swimming pool may occur gradually over a long period of time before it is discovered. Likewise, subsidence damage and cracking due to faulty construction may occur over several years before the insured becomes concerned. California courts have developed the manifestation rule (see §13.80) to determine which of several successive property insurance policies apply to continuous or progressive damage.

© The Regents of the University of California

§13.80 a. Manifestation Rule

Under the manifestation rule, the insurer on the risk at the time of appreciable damage that is or should be known to the insured is liable for the entire progressive loss (see §13.79) discovered or undiscovered during the policy period. Insurers that issue policies after "initial manifestation" of a loss bear no responsibility for claims related to that loss. *Larkspur Isle Condominium Owners' Ass'n, Inc. v Farmers Ins. Group* (1994) 31 CA4th 106, 110, 37 CR2d 3; *Sapiro v Encompass Ins.* (ND Cal 2004) 221 FRD 513, 518. Preexisting defects that do not manifest themselves before commencement of the policy term, but manifest during the policy term, are covered under a first party property policy unless otherwise excluded by the terms of the policy. *Prudential-LMI Commercial Ins. v Superior Court* (1990) 51 C3d 674, 699, 274 CR 387. "Manifestation" refers to when the damage first becomes apparent, *i.e.,* when a reasonable insured would be on notice of a potential insured loss. 51 C3d at 688; *Home Ins. Co. v Landmark Ins. Co.* (1988) 205 CA3d 1388, 1392, 253 CR 277. See §13.94. The presence of cracking, separations, or other problems such as stucco cracks or sticking doors may not establish the presence of "appreciable damage" such that a reasonable insured would be on notice of a potentially insured loss as a matter of law. The insured's testimony that he did not understand the significance of the signs, that he thought them to be ordinary wear and tear, will support a finding of the absence of the requisite "appreciable knowledge." *Tomaselli v Transamerica Ins. Co.* (1994) 25 CA4th 1269, 1279, 31 CR2d 433. However, if the insured retains an expert who discovers "appreciable damage," knowledge of the manifestation of the loss is imputed to the insured. *Sapiro v Encompass Ins.* (ND Cal 2004) 221 FRD 513, 519.

© The Regents of the University of California

§13.81 b. Fortuity

For a risk of loss to be the subject of insurance, it must have been a contingent or unknown event at the time the policy was issued. Insurance Code §22 states that "[i]nsurance is a contract whereby one undertakes to indemnify another against loss, damage, or liability arising from a contingent or unknown event."

Section 22 is included in every insurance policy issued in California as a matter of law. See *Metropolitan Life Ins. Co. v State Bd. of Equalization* (1982) 32 C3d 649, 654, 186 CR 578; *Truta v Avis Rent-A-Car Sys.* (1987) 193 CA3d 802, 812, 238 CR 806. The court in *Compagnie de Bauxites de Guinee v Insurance Co. of N. Am.* (3d Cir 1983) 724 F2d 369, 372 (quoting Restatement of Contracts §291, Comment a (1932)), stated that a fortuitous event is

> [a]n event which so far as the parties to the contract are aware is dependent on chance. It may be beyond the power of any human being to bring the event to pass; it may be within the control of third persons, it may even be a past event, such as the loss of vessel, provided that the fact is unknown to the parties.

The key to a fortuitous event is the insured's knowledge. Fortuity is determined by the subjective view of the insured. *Chadwick v Fire Ins. Exch.* (1993) 17 CA4th 1112, 1119, 21 CR2d 871. A loss may be inevitable at the time the policy is issued, but coverage for that loss is proper as long as the insured does not know at the time of applying for the policy that the loss will occur. *Snapp v State Farm Fire & Cas. Co.* (1962) 206 CA2d 827, 24 CR 44. Conversely, a party cannot purchase insurance at a time when he or she knows that forces have been set in motion that will inevitably lead to a later loss, because it is not fortuitous. *Insurance Co. of N. Am. v United States Gypsum Co.* (4th Cir 1989) 870 F2d 148, 153. In short, "it is against public policy to allow insurance coverage on a certainty." *InterMetal Mexicana v Insurance Co. of N. Am.* (3d Cir 1989) 866 F2d 71, 77.

In *Sabella v Wisler* (1963) 59 C2d 21, 27 CR 689, the carrier contended that a homeowner's policy did not cover a loss, because at the time the policy was issued, subsidence damage to the home was inevitable. The supreme court rejected the idea that inevitability was the sole test of fortuity. Any contingent or unknown event, including a past event, may be insured against. Ins C §250. See also *Snapp v State Farm Fire & Cas. Co.* (1962) 206 CA2d 827, 830, 24 CR 44 ("[After] any movement of land has occurred it might be said to have been 'inevitable' with semantic correctness, but such 'inevitability' does not alter the fact that at the time the contract of insurance was entered into, the event was only a *contingency* or *risk* that might or might not occur within the term of the policy").

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.82 c. 'Loss in Progress' Doctrine

§13.82 c. "Loss in Progress" Doctrine

The concept of a risk or peril that is the proper subject of insurance is codified in Ins C §250, which states:

> Except as provided in this article any contingent or unknown event, whether past or future, which may damnify a person having an insurable interest, or create a liability against him, may be insured against, subject to the provisions of this code.

For coverage to be found, however, a loss must generally be the result of the occurrence of a covered peril during the policy period. For most claims, this issue presents no problem. But for certain losses, such as losses involving earth movement, pollution, dry rot, or in which physical damage is suffered over time, this issue can be difficult.

In *Prudential-LMI Commercial Ins. v Superior Court* (1990) 51 C3d 674, 699, 274 CR 387, the court held that the "inception" of a progressive loss occurs when the damage is "manifested," *i.e.,* when appreciable damage occurs such that a reasonable person would be on notice of a potentially insured loss. See §13.80 on manifestation and §13.94 on inception of loss. Because it had earlier adopted a "reasonable insured" standard for the notice test (see §13.94), the court implied that the same standard should be applied to the manifestation of a "loss in progress." 51 C3d at 699.

However, the interpretation of when the loss is "manifested" depends on whether the policy is an "all-risk" or a "named-perils" policy. For example, in *Larkspur Isle Condominium Owners' Ass'n, Inc. v Farmers Ins. Group* (1994) 31 CA4th 106, 111, 37 CR2d 3, the court held that under an all-risk policy, the date of manifestation does not depend on the insured's knowledge that the damage may constitute a covered loss. In contrast, in *Central Nat'l Ins. Co. v Superior Court* (1992) 2 CA4th 926, 3 CR2d 622, the court applied the definition of "inception of the loss" set out in *Prudential-LMI* to a case involving a named-peril policy. In denying the insurer's petition for a writ, the court held that under a named-peril policy (in contrast to the all-risk policy in *Prudential-LMI*), the insured has no duty to make a claim under the policy until he or she has reason to know (1) that appreciable damage has occurred, and (2) that the damage was caused by a peril specified in the policy. The court held that it was an issue of fact whether the *Prudential-LMI* rule should apply, because the loss in *Prudential-LMI* was continuing and progressive and the loss in *Central Nat'l Ins.,* by the insured's own declaration, was not. Rather, it was the result of a series of discrete events, some of which occurred when the insurer was on the risk. If the damage was not continuous, but caused by a series of separate events, each successive insurer is liable only for the damage that occurred during the years it was on the risk. 2 CA4th at 933.

The ruling in *Prudential-LMI* that continuous property damage occurs on a single date of loss, the date of "manifestation," is limited to first party cases and is inapposite in the context of third party liability policies. Addressing the question left open in *Prudential-LMI,* the supreme court held in *Montrose Chem. Corp. v Admiral Ins. Co*. (1995) 10 C4th 645, 42 CR2d 324, that the "continuous injury trigger" was the appropriate standard to apply to continuous or progressively deteriorating losses covered by third party commercial general liability policies. Thus, third party losses continuing over more than one policy period are potentially covered by all policies in effect during those periods.

When progressive but undiscovered damage occurs during successive policy periods, *Prudential-LMI* appears to stand for the proposition that the carrier on the risk on the date of manifestation is solely responsible for the loss, including damages suffered after the policy period expires. Conversely, insurers whose policy period commences after initial manifestation of the loss are not responsible for any claim relating to the previously discovered and manifested loss. *Prudential-LMI Commercial Ins. v Superior Court* (1990) 51 C3d 674, 699, 274 CR 387. The "loss in progress" rule codifies a fundamental principle of insurance law, *i.e.,* that an insurer cannot insure against a loss that is known or apparent to the insured. "[S]ince an insurer may only insure against contingent or unknown risks of loss, a policy issued after the 'loss in progress' has begun does not cover such loss." *Pines of La Jolla Homeowners Ass'n v Industrial Indem.* (1992) 5 CA4th 714, 721, 7 CR2d 53. For a further discussion of the manifestation and the continuous injury theories, see California Liability Insurance Practice: Claims & Litigation §§3.38-3.39 (Cal CEB 1991).

© The Regents of the University of California

§13.83 3. Concurrent Causation and Efficient Proximate Cause

In *Garvey v State Farm Fire & Cas. Co.* (1989) 48 C3d 395, 403, 257 CR 292, the supreme court adopted the efficient proximate cause doctrine as the proper rule to apply when a loss is caused by the interaction of covered and excluded perils. Under the efficient proximate cause doctrine, "[w]hen a loss is caused by a combination of a covered and specifically excluded risks, the loss is covered if the covered risk was the efficient proximate cause of the loss," but "the loss is not covered if the covered risk was only a remote cause of the loss, or the excluded risk was the efficient proximate, or predominate cause." *State Farm Fire & Casualty Co. v Von Der Lieth* (1991) 54 C3d 1123, 1131, 2 CR2d 183. The efficient proximate cause of a loss is the "predominating cause" or "most important" cause of the loss. See also *Julian v Hartford Underwriters Ins. Co*. (2005) 35 C4th 747, 754, 27 CR3d 648; *Freedman v State Farm Ins. Co.* (2009) 173 CA4th 957, 961, 93 CR3d 296.

If more than one peril contributes to a loss, the question of the efficient proximate cause is generally a factual matter for the jury to resolve. *Garvey,* 48 C3d at 413. However, when all of the perils contributing to the loss are excluded under the policy, judgment can be entered for the insurer as a matter of law. *Brodkin v State Farm Fire & Cas. Co.* (1989) 217 CA3d 210, 217, 265 CR 710.

For the "efficient proximate cause" theory to apply, there must be two separate and distinct perils that "could each, under some circumstance, have occurred independently of the other and caused damage." When the evidence shows the loss was in fact occasioned by only a single cause, albeit one susceptible to various characterizations, the "efficient proximate cause" analysis has no application. *Roberts v Assurance Co. of Am.* (2008) 163 CA4th 1398, 1410, 78 CR3d 361 (policy excluded coverage for earth movement; concealment of ancient landslide was not conceptually distinct peril from ancient landslide itself); *Chadwick v Fire Ins. Exch.* (1993) 17 CA4th 1112, 1117, 21 CR2d 871 (policy excluded coverage for latent defects in construction; negligent construction just separate characterization, not distinct peril).

Several appellate courts have faced the issue of whether a property insurer may contractually exclude coverage when a covered peril is the efficient proximate cause of the loss but an excluded peril has contributed to or was necessary to the loss. In *Julian v Hartford Underwriters Ins. Co*. (2005) 35 C4th 747, 27 CR3d 648, a policy exclusion sought to preclude coverage for losses caused by weather conditions that "contribute in any way with" an excluded cause or event, such as a landslide. 35 C4th at 750. The California Supreme Court noted that the phrase "contributed in any way with" seemed "particularly designed to circumvent the efficient proximate cause doctrine." 35 C4th at 760. The court indicated that such a provision would not be enforceable if 99 percent of the loss was caused by weather conditions and 1 percent by earth movement. 35 C4th at 760. However, the court expressly limited its holding to the application of the weather conditions clause to a loss caused by a rain-induced landslide, and held that the exclusion was enforceable to the extent weather conditions were the efficient proximate cause of the loss. 35 C4th at 760. The court held that the exclusion, as so interpreted, did not violate Ins C §530 or the "efficient proximate cause" doctrine. 35 C4th at 761. The court stated that the efficient proximate cause doctrine does not preclude an insurer from providing coverage for some, but not all, of the manifestations of a peril, as long as the policy makes clear which perils are and are not covered. 35 C4th at 759.

In *DeBruyn v Superior Court* (2008) 158 CA4th 1213, 1216, 70 CR3d 652, the appellate court applied *Julian* and held that an "all risk" policy that "plainly and precisely communicated" that mold damage is not covered even when it results from a covered peril did not violate Ins C §530 or the efficient proximate cause doctrine. See §13.130. In *Freedman v State Farm Ins. Co.* (2009) 173 CA4th 957, 962, 93 CR3d 296 the appellate court applied *Julian* to hold that an "all risk" policy that excludes coverage for damage caused by "third party negligence," "corrosion," and "continuous seepage or leakage of water" from a plumbing system, excludes "contractor-negligence-induced" corrosion and "continuous or repeated seepage or leakage of water."

Distinct from the issue of concurrent causation is the situation in which a covered peril (such as fire) results from an excluded peril (such as earthquake). The policy language often provides coverage to the extent the loss is caused by the resulting, and covered, peril. See §13.84.

© The Regents of the University of California

VII. COMMON EXCLUSIONS

§13.84 A. Exclusions, Ensuing Losses, and Efficient Proximate Cause

The term "ensuing loss" refers to a situation in which two perils, one excluded and one not excluded, combine to cause damage. If a subsequent peril causes a loss or injury separate and independent but resulting from the original excluded peril, and this new peril is not excluded under the policy, the loss or injury caused by the subsequent, unexcluded peril is an "ensuing loss." See, *e.g.*, *Sapiro v Encompass Ins.* (ND Cal 2004) 221 FRD 513, 522. Thus, a determination that damage was caused by an excluded peril does not mean all loss resulting from it is excluded. Further analysis is necessary to determine whether the loss, or part of the loss, was caused by an "ensuing loss."

Commercial property policies that provide "all risk" coverage formerly used the term "ensuing loss," and stated that "any ensuing loss to property described in Coverages A and B not excluded or excepted in this policy is covered." This led courts to hold that damage caused by an "ensuing loss" was not excluded. For example, in *Pacific Heating & Ventilating Co. v Williamsburg City Fire Ins. Co*. (1910) 158 C 367, 111 P 4, the court held that even though the fire policy excluded damage caused by earthquake, when a fire started after the earthquake, damage caused by the fire was covered.

In response to the ensuing loss rule, insurers have removed the ensuing loss language from most policies. The ISO Causes of Loss—Special Form (CP 10 30 04 02) does not use the term "ensuing loss." Rather, it uses somewhat similar language in regard to only three exclusions: weather conditions; governmental decisions; and faulty planning, design, materials, or maintenance. See §13.86. The form states (here, items 3.a-3.c refer to the preceding excluded perils):

> We will not pay for loss or damage caused by or resulting from any of the following: 3.a. through 3.c. But if an excluded cause of loss that is listed in 3.a. through 3.c. results in a Covered Cause of Loss, we will pay for the loss or damage caused by that Covered Cause of Loss.

Under the efficient-proximate-cause doctrine, when there is a concurrence of two different causes, the efficient cause —the one that sets the others in motion—is the cause to which the loss is to be attributed, although other causes may follow it and operate more immediately in producing the disaster. *Garvey v State Farm Fire & Cas. Co.* (1989) 48 C3d 395, 402, 257 CR 292. If the efficient proximate cause is one or more covered perils in combination with specifically excluded risks, the coverage will apply. *State Farm Fire & Cas. Co. v Von Der Lieth* (1991) 54 C3d 1123, 1133, 2 CR2d 183. See discussion in §13.83.

Some carriers have argued that language in an exclusion barring coverage for loss "resulting from, contributed to or aggravated by" the excluded cause manifests an intent to void the application of the efficient-proximate-cause analysis and eliminates coverage. This theory has been rejected. *Howell v State Farm Fire & Cas. Co.* (1990) 218 CA3d 1446, 1457, 267 CR 708; *Mission Nat'l Ins. Co. v Coachella Valley Water Dist.* (1989) 210 CA3d 484, 496, 258 CR 639.

© The Regents of the University of California

§13.85 B. List of Common Exclusions

The most important exclusions from coverage are contained in the ISO Covered Causes of Loss—Special Form (CP 10 30 04 02) and the ISO Covered Causes of Loss—Broad Form (CP 10 20 04 02), with some overlap. See §13.86 (Special Form exclusions) and §13.87 (Special and Broad Form exclusions).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.86 1. Exclusions From Special Form (CP 10 30 04 02)

§13.86 1. Exclusions From Special Form (CP 10 30 04 02)

The ISO Covered Causes of Loss—Special Form (CP 10 30 04 02) excludes loss from the following perils:

- *Weather Conditions.* This exclusion applies only if weather conditions, in conjunction with another cause or event, contribute to produce the loss or damage. See discussion of *Julian v Hartford Underwriters Ins. Co.* (2005) 35 C4th 747, 27 CR3d 648, in §13.83.
- *Governmental Decisions*. The form excludes coverage for "governmental acts or decisions," including the failure to act or decide, of any person, group, organization, or governmental body. See *Waldsmith v State Farm Fire & Cas. Co.* (1991) 232 CA3d 693, 283 CR 607 (damage caused by landslide caused by saturated soil caused by broken water main was not covered, because earth movement and city's negligence were both excluded perils).
- *Faulty Planning, Design, Materials, or Maintenance*. The Special Form (CP 10 30 04 02) states this exclusion as follows:

  c. Faulty, inadequate or defective:
  (1) Planning, zoning, development, surveying, siting;
  (2) Design, specifications, workmanship, repair, construction, renovation, remodeling, grading, compaction;
  (3) Materials used in repair, construction, renovation or remodeling; or
  (4) Maintenance;
  of part or all of any property on or off the described premises.

EXAMPLE: See *Wilson v Farmers Ins. Exch.* (2002) 102 CA4th 1171, 126 CR2d 305, in which the court denied the mortgagor's claim for the decrease in the value of a home acquired through foreclosure when the named-insured mortgagee abandoned a renovation and defaulted on the loan. The court held that the unfinished renovation fell within the scope of the "inadequate renovation" exclusion of an all-risk homeowner's insurance policy. See also *Freedman v State Farm Ins. Co.* (2009) 173 CA4th 957, 93 CR3d 296 (similar exclusion precluded coverage for damage resulting from contractor negligence in driving nail through wall into water pipe, which corroded, then leaked, causing damage and mold); *Davis v United Servs. Auto. Ass'n* (1990) 223 CA3d 1322, 273 CR 224 (exclusion applies to contractor negligence); *Mission Nat'l Ins. Co. v Coachella Valley Water Dist.* (1989) 210 CA3d 484, 258 CR 639 (jury issue about which of two causes is efficient cause); *Sapiro v Encompass Ins.* (ND Cal 2004) 221 FRD 513, 521 (exclusion precluded coverage for damage caused by moisture, water damage, and fungi resulting from gap between flashing and stucco of home; water damage and fungal growth were not ensuing losses because they were not separate and independent from the original peril).

- *Delay, Loss of Use, or Loss of Market*. The form excludes loss or damage caused by or resulting from delay, loss of use, or loss of market.
- *Smoke, Vapor, or Gas*. The form excludes loss or damage caused by or resulting from smoke, vapor, or gas from agricultural smudging or industrial operations.
- *Wear and Tear*. The form excludes loss or damage caused by or resulting from (1) wear and tear; (2) rust or other corrosion, decay, deterioration, hidden or latent defect, or any quality in property that causes it to damage or destroy itself; (3) smog; (4) settling, cracking, shrinking, or expanding; and (5) nesting or infestation, or discharge or release of waste products or secretions, by insects, birds, rodents, or other animals. However, if an excluded cause of loss results in a "specified cause of loss" or building glass breakage, the exclusion will not apply to loss or damage caused by that "specified cause of loss" or building glass breakage. See *Scott v Continental Ins. Co.* (1996) 44 CA4th 24, 35, 51 CR2d 566 (latent defect must be not readily observable and also difficult to discover; latent defect and inherent vice exclusions apply to faults, flaws, and irregularities in design, faulty construction, or weakness of materials); *Chadwick v Fire Ins. Exch*. (1993) 17 CA4th 1112, 1126, 21 CR2d 871 (latent defect means not apparent by reasonable inspection); *Murray v State Farm Fire & Cas. Co*. (1990) 219 CA3d 58, 268 CR 33 (deterioration of copper water pipe caused by electrolysis over 17-year period, when expected to last 50 years, excluded as wear and tear); *Brodkin v State Farm Fire & Cas. Co.* (1989) 217

CA3d 210, 217, 265 CR 710 (slow disintegration of concrete foundation because of corrosive soil conditions is excluded deterioration).

- *Dampness, Dryness, Changes or Extremes in Temperature*. The form excludes loss or damage to personal property caused by or resulting from dampness or dryness of atmosphere, or changes in or extremes of temperature. However, if an excluded cause of loss results in a "specified cause of loss" or building glass breakage, the exclusion will not apply to loss or damage caused by that "specified cause of loss" or building glass breakage.
- *Continuous or Repeated Seepage or Leakage of Water*. The form excludes loss or damage caused by or resulting from continuous or repeated seepage or leakage of water, or the presence or condensation of humidity, moisture, or vapor, that occurs over a period of 14 days or more. See *Freedman v State Farm Ins. Co.* (2009) 173 CA4th 957, 93 CR3d 296 (exclusion for continuous or repeated seepage or leakage of water from plumbing system whether it arises from natural or external causes precluded coverage for damage resulting from contractor negligence, causing damage and mold); *Finn v Continental Ins. Co*. (1990) 218 CA3d 69, 72, 267 CR 22 (exclusion applies to gradual disintegration over time, not sudden and accidental rupture or leak).
- *Freezing*. The form excludes loss or damage caused by or resulting from water, other liquids, powder, or molten material that leaks or flows from plumbing, heating, air-conditioning, or other equipment (except fire protection systems) caused by or resulting from freezing, unless (1) the insured does its best to maintain heat in the building or structure; or (2) the insured drains the equipment and shuts off the supply if the heat is not maintained. See *Waldsmith v State Farm Fire & Cas. Co.* (1991) 232 CA3d 693, 697, 283 CR 607 (exclusion refers to plumbing, heating, air-conditioning, or other equipment within or part of the building, not city water main).
- *Dishonest or Criminal Acts*. The form excludes loss or damage caused by or resulting from dishonest or criminal acts by the insured, any of the insured's partners, members, officers, managers, employees (including lease employees), directors, trustees, authorized representatives, or anyone to whom the insured entrusts the property for any purpose, whether acting alone or in collusion with others, or whether or not occurring during the hours of employment. See *Safeco Ins. Co. v Robert S.* (2001) 26 C4th 758, 110 CR2d 844 (exclusion for "illegal acts" overbroad and unenforceable in wrongful death action for accidental shooting (interpreting liability policy)); *20th Century Ins. Co. v Schurtz* (2001) 92 CA4th 1188, 112 CR2d 547 (criminal act exclusion applies regardless of insured's intent (interpreting liability policy); *20th Century Ins. Co. v Stewart* (1998) 63 CA4th 1333, 74 CR2d 492 (pointing gun and pulling trigger, despite belief that gun will not fire, shows disregard for human life and establishes implied malice (interpreting liability policy)). This exclusion does not apply to acts of destruction by the insured's employees (including leased employees), but it does apply to theft by employees (including leased employees).
- *Voluntary Parting*. The form excludes loss or damage caused by or resulting from voluntary parting with any property by the insured, or anyone else to whom the insured has entrusted the property, if induced to do so by any fraudulent scheme, trick, device, or false pretense. See *EOTT Energy Corp. v Storebrand Int'l Ins. Co.* (1996) 45 CA4th 565, 573, 52 CR2d 894 (exclusion does not apply when theft was accomplished by physically disabling fuel meters, rather than "voluntary parting").
- *Rain, Snow, Ice, or Sleet*. The form excludes loss or damage caused by or resulting from rain, snow, ice, or sleet to personal property in the open. See *Palub v Hartford Underwriters Ins. Co.* (2001) 92 CA4th 645, 648, 112 CR2d 270 (to extent all-risk policy excludes loss proximately caused by weather conditions (*e.g.,* rain), it violates Ins C §530 regarding efficient proximate cause and is unenforceable).
- *Collapse*. The form excludes loss or damage caused by or resulting from collapse, except as provided in the Additional Coverage for Collapse. However, if collapse results in a covered cause of loss at the described premises, the exclusion does not apply to loss or damage caused by that covered cause of loss. Collapse is not a cause of loss under an all-risk policy, but is the damage itself. See *Palub v Hartford Underwriters Ins. Co.* (2001) 92 CA4th 645, 648, 112 CR2d 270; see also *Stamm Theatres, Inc. v Hartford Cas. Ins. Co.* (2001) 93 CA4th 531, 113 CR2d 300 (coverage for collapse resulting from "hidden decay" applied to unexpected failure of roof trusses having no apparent evidence of deterioration); *Doheny W. Homeowners' Ass'n v American Guar. & Liab. Ins. Co*. (1997) 60 CA4th 400, 70 CR2d 260 (policy that covered loss or damage "involving collapse" afforded coverage for actual or imminent collapse); but see *Rosen v State Farm Gen. Ins. Co.* (2003) 30 C4th

1070, 135 CR2d 361 (policy defining "collapse" as "actually fallen down or fallen into pieces" required actual collapse and could not be interpreted as affording coverage for imminent collapse on public policy grounds); *Jordan v Allstate Ins. Co.* (2004) 116 CA4th 1206, 11 CR3d 169 *(Jordan I)* (exclusion for "wet or dry rot" was ambiguous under provisions regarding additional coverage for collapse caused by "hidden decay," but court held that policy required actual collapse, not danger of collapse or "imminent collapse"); and *Jordan v Allstate Ins. Co.* (2007) 148 CA4th 1062, 56 CR3d 312 *(Jordan II)* (insurer failed to conduct a "full, fair, thorough and timely" investigation of the alleged collapse).

- *Pollutants*. The form excludes loss or damage caused by or resulting from the discharge, dispersal, seepage, migration, release, or escape of "pollutants" unless the discharge, dispersal, seepage, migration, release, or escape is itself caused by any of the "specified causes of loss." However, if the discharge, dispersal, seepage, migration, release, or escape of "pollutants" results in a "specified cause of loss," the coverage will apply to loss or damage caused by that "specified cause of loss." See *Brian Chuchua's Jeep, Inc. v Farmers Ins. Group* (1992) 10 CA4th 1579, 13 CR2d 444 (cleanup expenses from underground gas tank leak caused by earthquake covered under earthquake coverage, notwithstanding pollution exclusion). Further, this exclusion does not apply to damage to glass caused by chemicals applied to that glass. In *McKinnon v Truck Ins. Exch.* (2003) 31 C4th 635, 653, 3 CR3d 228, the California Supreme Court held that the term "pollutant" in the absolute pollution exclusion in a CGL policy is limited to "conventional environmental pollution," and did not encompass "ordinary acts of negligence involving harmful substances," such as the negligent application of pesticides. See also *Garamendi v Golden Eagle Ins. Co.* (2005) 127 CA4th 480, 485, 25 CR3d 642 (widespread dissemination of silica dust as incidental by-product of industrial sandblasting is "environmental pollution"). For further discussion of pollution coverage, see §§13.45-13.51.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.87 2. Exclusions From Special Form (CP 10 30 04 02) and Broad Form (CP 10 20 04 02)

§13.87 2. Exclusions From Special Form (CP 10 30 04 02) and Broad Form (CP 10 20 04 02)

Both the ISO Special Form (CP 10 30 04 02) and the ISO Broad Form (CP 10 20 04 02) exclude loss from the following perils:

- *Ordinance or Law Exclusion*. The forms exclude coverage for loss or damage caused directly or indirectly by the enforcement of any ordinance or law (1) regulating the construction, use, or repair of any property, or (2) requiring the tearing down of any property, including the cost of removing its debris. This exclusion applies whether the loss results from (a) an ordinance or law that is enforced even if the property has not been damaged, or (b) the increased costs incurred to comply with an ordinance or law in the course of construction, repair, renovation, remodeling, or demolition of property following a physical loss to that property. See *Bischel v Fire Ins. Exch.* (1991) 1 CA4th 1168, 2 CR2d 575 (cost of construction upgrades required by ordinances or law must be borne by insured); *McCorkle v State Farm Ins. Co.* (1990) 221 CA3d 610, 270 CR 492; *Breshears v Indiana Lumbermens Mut. Ins. Co.* (1967) 256 CA2d 245, 63 CR 879. An exclusion that does not substantially comply with the "ordinance or law" exclusionary language in Ins C §2071, however, may be found to be ambiguous and not given effect. *Fire Ins. Exch. v Superior Court* (2004) 116 CA4th 446, 10 CR3d 617.
- *Earth Movement*. The forms exclude coverage for loss or damage caused directly or indirectly by earthquake, landslide, mine subsidence, and earth sinking, other than sinkhole collapse. However, if these perils result in fire or explosion, the insurance will cover damage caused by that fire or explosion. Both forms also exclude loss or damage caused directly or indirectly by volcanic eruption, even if it results in fire damage. See also *Roberts v Assurance Co. of Am.* (2008) 163 CA4th 1398, 1406, 78 CR3d 361 (exclusion for "earth movement" in course of construction from builder's risk policy precluded coverage for landslide damage to insured's house resulting from movement of ancient landslide below property, activated by placement of fill soil on adjoining lot and insured's lot during grading before construction, in combination with heavy rains).
- *Governmental Action.* The forms exclude coverage for loss or damage caused directly or indirectly by seizure or destruction of property by order of governmental authority. The policy will apply, however, to loss or damage caused by or resulting from acts of destruction ordered by governmental authority and taken at the time of a fire to prevent its spread, if the fire damage would otherwise be covered.
- *Nuclear Hazard.* The forms exclude coverage for loss or damage caused directly or indirectly by nuclear reaction or radiation, or radioactive contamination, however caused. If nuclear reaction or radiation or radioactive contamination results in fire, the exclusion does not apply to loss or damage caused by such fire.
- *Utility Services*. The forms exclude coverage for loss or damage caused directly or indirectly by the failure of power or other utility service supplied to the destroyed premises, however caused, if the failure occurs away from the described premises. If the failure of power or other utility service results in a covered cause of loss, the exclusion will not apply to damage or loss caused by that covered cause of loss. This exclusion does not apply to business income coverage or extra expense coverage.
- *War and Military Action*. The forms exclude coverage for loss or damage caused directly or indirectly by (1) war, including undeclared or civil war; (2) warlike action by a military force; and (3) insurrection, rebellion, revolution, usurped power, or action taken by governmental authority in hindering or defending against any of these.
- *Water.* The forms exclude coverage for loss or damage caused directly or indirectly by (1) flood, surface water, waves, tides, tidal waves, or overflow of any body of water; (2) mudslide or mudflow; (3) water that backs up or overflows from a sewer, drain, or sump; or (4) water under the ground surface pressing on or flowing or seeping through foundations, walls, floors or paved surfaces, basements, or doors, windows, or other openings. However, if such water results in fire, explosion, or sprinkler leakage, the exclusion will not apply to damage caused by such fire, explosion, or sprinkler leakage.

NOTE: A 2004 report by the California Department of Insurance found that 41 percent of multi-peril homeowners insurers use water-loss exclusions or special limits for losses caused by water.

In *Penn-America Ins. Co. v Mike's Tailoring* (2005) 125 CA4th 884, 22 CR3d 918, the court held that the sewer backup exclusion is not facially ambiguous and that it precluded coverage for damage caused when a clogged sewer line caused water and sewage to flow into the basement of the insured property. The court rejected the insured's argument that the loss was covered because it was caused by a pollutant (sewage), holding that a reasonable layperson would assume water backing up from a sewer would contain both water and contaminants. 125 CA4th at 890.

Damage caused by water intrusion in a gap between the flashing and stucco of a home falls within the water damage exclusion. *Sapiro v Encompass Ins*. (ND Cal 2004) 221 FRD 513, 522.

Damage to an insured shipyard from coverage with ten feet of water from Hurricane Katrina was held to be within the flood exclusion of an excess policy in *Northrup Grumman Corp. v Factory Mut. Ins. Co.* (9th Cir 2009) 563 F3d 777, 783. In addition to the definition of "flood" in the policy, the court considered dictionary definitions, which characterize "flood" as an overflowing or inundation of water over usually dry land. *Northrup* at 783.

- *Fungus, Wet Rot, Dry Rot, and Bacteria.* The forms exclude coverage for loss or damage caused directly or indirectly by the presence, growth, proliferation, spread, or any activity of fungus, wet or dry rot, or bacteria. However, if fungus, wet or dry rot, or bacteria result in a covered cause of loss, damage caused by that covered cause of loss will be covered. Further, this exclusion does not apply when fungus, wet or dry rot, or bacteria results from fire or lightning. With respect to loss or damage caused by a covered cause of loss other than fire or lightning, the exclusion does not apply to the extent that coverage is provided in the Additional Coverage—Limited Coverage for "Fungus," Wet Rot, Dry Rot, and Bacteria (CP 10 30 04 02, §E, p 7; CP 10 20 04 02, §D, p 6). See also §13.130. The exclusion precludes coverage for decay caused by fungus. *Sapiro v Encompass Ins.* (ND Cal 2004) 221 FRD 513, 522. The exclusion for "wet or dry rot" precludes coverage for decay caused by a fungus. But see *Jordan v Allstate Ins. Co.* (2004) 116 CA4th 1206, 1218, 11 CR3d 169 *(Jordan I)* (finding ambiguity between that exclusion and additional coverage for collapse caused by hidden decay).
- *Artificially Generated Electrical Current*. The forms exclude coverage for loss or damage caused by or resulting from artificially generated electrical current.
- *Explosion of Steam Boilers, Pipes, or Turbines*. The forms exclude coverage for loss or damage caused directly or indirectly by explosion of steam boilers, steam pipes, steam engines, or steam turbines owned or leased by the insured, or operated under the insured's control.
- *Mechanical Breakdown*. The forms exclude coverage for loss or damage caused directly or indirectly by mechanical breakdown, including rupture or bursting caused by centrifugal force. However, if mechanical breakdown results in a covered cause of loss, this exclusion does not apply to damage caused by that covered cause of loss.
- *Insured's Neglect*. The forms exclude coverage for loss or damage caused directly or indirectly by an insured's neglect to use all reasonable means to save and preserve property from further damage at and after the time of loss.

© The Regents of the University of California

VIII. WHAT TO DO WHEN A LOSS OCCURS: CONDITIONS

§13.88 A. Notice to Insurance Company

Most property insurance policies contain fairly detailed instructions on the insured's duties after a loss. The instructions are based on Ins C §2071, which sets forth a Standard Form Fire Policy. The substance of that form is found in nearly every property insurance policy, whether residential or commercial, issued in California. The loss-adjustment provisions of §2071 provide two important requirements on notice:

- The insured must give written notice to the insurer of any loss without unnecessary delay.
- The insured must file, *within 60 days after the loss* unless the time is extended in writing by the insurer, a *proof of loss,* signed and sworn to by the insured, stating the insured's knowledge and belief about certain matters set forth in Ins C §2071 (see §13.89).

These time limits normally run from the inception of the loss. See §13.94 for further discussion of "inception of the loss."

Although it is prudent for the insured to provide prompt notice of loss, a delay in providing notice will not, in the absence of substantial prejudice to the insurer, support a refusal to pay. See *Northwestern Title Sec. Co. v Flack* (1970) 6 CA3d 134, 85 CR 693 (claim on professional errors and omissions policy).

NOTE: After the insured incurs a covered loss, the insurer must provide a free copy of the policy within 30 days after receipt of a request from the insured. Ins C §2071(a).

© The Regents of the University of California

§13.89 B. Proof of Loss

Generally, insurance policies impose a duty on the insured to provide proof of the loss. The Standard Form Fire Policy states that the insured must file, *within 60 days after the loss* unless the time is extended in writing by the insurer, a *proof of loss,* signed and sworn to by the insured, stating the insured's knowledge and belief about certain matters set forth in Ins C §2071, including the following:

- The time and origin of the loss;
- The interest of the insured and all others in the property;
- The actual cash value of each item and amount of loss thereto;
- All encumbrances on the property;
- All other contracts of insurance on the property, whether valid or not;
- Any changes in the title, use, occupation, location, possession, or exposures of the property since the policy was issued;
- By whom and for what purpose any building was occupied at the time of loss; and
- Whether or not the building stood on leased ground.

The insured must also provide a copy of all descriptions and schedules in all policies and, if required and obtainable, verified plans and specifications of any building, fixtures, or machinery destroyed or damaged.

The insured is not required to provide the type or quality of proof that might be required in court; it is sufficient for the insured to give "the best evidence in his power at the time." Ins C §552. If the insurer fails to promptly notify the insured of any defects in the proof of loss that the insured might remedy, the defect will be waived. Ins C §553.

© The Regents of the University of California

§13.90 C. Insured's Duty of Cooperation

Most policies require the insured to cooperate with the insurer's investigation of a claim. For example, the Standard Form Fire Policy states (Ins C §2071(a)):

> The insured, as often as may be reasonably required…, shall exhibit to any person designated by this company all that remains of any property herein described, and submit to examinations under oath by any person named by this company, and subscribe the same; and, as often as may be reasonably required, shall produce for examination all books of account, bills, invoices, and other vouchers….

An insured's refusal to cooperate will be a defense to coverage only if the insurer is prejudiced as a result. *Pruyn v Agricultural Ins. Co.* (1995) 36 CA4th 500, 516, 42 CR2d 295. Moreover, the insurer has the burden of proving that it was prejudiced by the insured's refusal to cooperate. 36 CA4th at 516.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.91 D. Insurer's Duty to Produce 'Claim-Related Documents'

§13.91 D. Insurer's Duty to Produce "Claim-Related Documents"

The Standard Form Fire Policy, codified in Ins C §2071, requires the insurer, on request from an insured, to produce "claim-related documents" within 15 days. This requirement also applies to any other "residential property insurance policies." "Claim-related documents" include:

- Repair and replacement estimates and bids;
- Appraisals and "scope of loss" documents;
- Drawings, plans, and reports;
- Third party findings on the amount of loss; and
- "All other valuation, measurement and loss adjustment calculations of the amount of loss, covered damage, and costs of repairs."

© The Regents of the University of California

§13.92 E. Examination Under Oath

Many property policies impose a duty on the insured to submit to an examination under oath (EUO). The Standard Form Fire Policy (Ins C §2071(a)) states:

> The insured, as often as may be reasonably required…, shall… submit to examinations under oath by any person named by this company, and subscribe the same….

Once requested, an EUO becomes a condition precedent to payment of the claim. *California Fair Plan Ass'n v Superior Court* (2004) 115 CA4th 158, 161, 8 CR3d 746. The insured cannot refuse to submit to an EUO on the ground that the insurer's purpose is to gather information to defeat the claim. *Hickman v London Assur. Corp.* (1920) 184 C 524, 530, 195 P 45; *Globe Indem. Co. v Superior Court* (1992) 6 CA4th 725, 731, 8 CR2d 251. The requirement that the insured "subscribe" the EUO indicates that it must be given under oath and taken down and transcribed by a court reporter; a previously recorded statement, or verbal assurances that the insured answered questions truthfully at an earlier interview, will not excuse the insured's duty to submit to an EUO. *West v State Farm Fire & Cas. Co.* (9th Cir 1988) 868 F2d 348, 351.

The insurer's right to conduct an EUO and to require the insured to produce documents is so significant that the insured's compliance is a prerequisite to the right to receive policy benefits. *Brizuela v Calfarm Ins. Co.* (2004) 116 CA4th 578, 587, 10 CR3d 661. In *Brizuela*, the court held that the insured's failure to attend the EUO as scheduled by the insurer, and failure to propose any alternative dates for the EUO for 6 months, legally constituted a refusal to submit to an EUO. Moreover, the court held that the insurer had no obligation to provide the insured with a copy of the insured's previously recorded statements before the EUO. The court held the insurer was not required to show prejudice before denying policy benefits to an insured who violated a policy provision requiring submission to an EUO. The court further held that the availability of a deposition in the bad faith litigation did not excuse the insured's breach of the policy regarding an EUO.

The EUO may be conducted only to obtain information that is "relevant and reasonably necessary to process or investigate the claim." Ins C §2071.1(a)(2). Moreover, the insurer may conduct the EUO only on reasonable notice, at a convenient place and for a reasonable length of time. Ins C §2071.1(a)(3). The insured has a right to be represented by counsel at the examination (Ins C §2071.1(a)(4)) and to receive a free copy of the transcript (Ins C §2071.1(a)(5)). Although the insured or his or her counsel may object to questions, if a refusal to answer a material question prevents the insurer from determining the extent of loss and validity of the claim, the insured's right to recover under the policy may be affected. Ins C §2071.1(a)(6) The insurer must provide a copy of Ins C §2071.1 along with its request to take the EUO. Ins C §2071.1(a)(1).

© The Regents of the University of California

F. Statute of Limitations

§13.93 1. 1-Year Limitations Period

A 1-year contractual statute of limitations period is permitted in property policies by Ins C §2071(a), which provides that

> [n]o suit or action on this policy for the recovery of any claim shall be sustainable in any court of law or equity unless all the requirements of this policy shall have been complied with, and unless commenced within 12 months next after inception of the loss.

Although this language is not mandatory (see Ins C §2079), it is included in virtually every property insurance policy issued in California. The 1-year statute of limitations has been held valid and enforceable. See *Prudential-LMI Commercial Ins. Co. v Superior Court* (1990) 51 C3d 674, 683, 274 CR 387 (recognizing reasonable delay in discovery and equitable tolling until insurer's formal denial of claim); *Shugerman v Allstate Ins. Co.* (CD Cal 2009) 594 F Supp 2d 1131, 1135. Some policies vary the language to require that suit be brought within 12 months after the "happening" or the "occurrence" of the loss, rather than the "inception" of the loss. See §13.94. However, the courts generally find that this language conforms to that in the standard form.

In accordance with the requirements of the Unfair Insurance Practices Act (Ins C §§790-790.15), the Fair Claims Practices Regulations (10 Cal Code Regs §§2695.1-2695.14) impose a mandatory duty on an insurer to disclose to a first party claimant any time limit that may apply to the claim. 10 Cal Code Regs §2695.4(a). If the insurer fails to do so, it will be estopped from relying on that time limit. *Neufeld v Balboa Ins. Co.* (2000) 84 CA4th 759, 764, 101 CR2d 151; *Spray, Gould & Bowers v Associated Int'l Ins. Co.* (1999) 71 CA4th 1260, 1264, 84 CR2d 552. An insurer may also be estopped from relying on the time limit if the insured can show that he or she reasonably relied on misrepresentations by the insurer that led to the insured's failure to file a timely claim. *Vu v Prudential Prop. & Cas. Ins. Co.* (2001) 26 C4th 1142, 1152, 113 CR2d 70; *Cordova v 21st Century Ins. Co.* (2005) 129 CA4th 89, 95, 28 CR3d 170; *Shugerman v Allstate Ins. Co.* (CD Cal 2009) 594 F Supp 2d 1131, 1140 (stating rule, but holding that communications after the limitations period expired may not form the basis for estoppel). Under 10 Cal Code Regs §2695.7(f), however, once the insurer accepts coverage, the insurer need not notify the insured of the applicable limitations period. See *SEMX Corp. v Federal Ins. Co.* (SD Cal 2005) 398 F Supp 2d 1103 (after insurer settled insured's initial first party claim, insurer was no longer bound to provide notice of policy's 2-year limitations period).

In *Hellinger v Farmers Ins. Exch.* (2001) 91 CA4th 1049, 1055, 111 CR2d 268, the court held that Ins C §2071 does not apply to stand-alone policies covering earthquake damage only. See also *Bialo v Western Mut. Ins. Co.* (2002) 95 CA4th 68, 75, 115 CR2d 3.

WARNING: Code of Civil Procedure §340.9 revives insurance claims resulting from the 1994 Northridge earthquake that were formerly time-barred by Ins C §2071, but does not apply to claims for damage caused by the earthquake's aftershocks. See *Migliore v Mid-Century Ins. Co.* (2002) 97 CA4th 592, 118 CR2d 548. However, the statute does not preclude the victims of the Northridge earthquake from asserting that the insurer is equitably estopped from relying on the statute of limitations. *Cordova v 21st Century Ins. Co.* (2005) 129 CA4th 89, 95, 28 CR3d 170. This statute does not revive claims compromised by a written settlement agreement if the insured was represented by counsel admitted to practice in California. *Israel-Curley v California Fair Plan* (2005) 126 CA4th 123, 128, 24 CR3d 1. Moreover, the statute does not affect any other defenses the insurer might have. *Rosenblum v Safeco Ins. Co.* (2005) 126 CA4th 847, 858, 24 CR3d 427.

© The Regents of the University of California

§13.94 2. Inception of the Loss

Before the litigation in *Prudential-LMI Commercial Ins. v Superior Court* (1990) 51 C3d 674, 274 CR 387, cases on the statute of limitations in property policies focused on two issues:

- In the context of the discovery of concealed damages, when was the inception of the loss?
- In the event of a protracted adjustment, could the statute be tolled by the insurer's actions?

Prudential-LMI addressed both issues. The supreme court held that a "reasonable person" standard must be applied to determine when a loss begins or occurs. The limitations period begins to run when a reasonable insured presumably has facts sufficient to require notifying the carrier of a claim (51 C3d at 687):

> We agree that "inception of the loss" should be determined by reference to reasonable discovery of the loss and not necessarily turn on the occurrence of the physical event causing the loss. Accordingly, we find that California law supports the application of the following delayed discovery rule for purposes of the accrual of a cause of action under [Ins C §] 2071: the insured's suit on the policy will be deemed timely if it is filed within one year after "inception of a loss," defined as that point in time when appreciable damage occurs and is or should be known to the insured, such that a reasonable insured would be aware that his notification duty under the policy has been triggered. To take advantage of the benefits of a delayed discovery rule, however, the insured is required to be diligent in the face of discovered facts. The more substantial or unusual the nature of the damage discovered by the insured (*e.g.,* the greater its deviation from what a reasonable person would consider normal wear and tear), the greater the insured's duty to notify his insurer of the loss promptly and diligently.

Further, the time when a reasonable insured "would be on notice of a potentially insured loss" is usually an issue of fact, which cannot always be determined on a motion for summary judgment. 51 C3d at 687. Finally, the 1-year statute of limitations is a defense that the insurer must raise, and the insurer alone has the burden of proof. 51 C3d at 687. See also *Kapsimallis v Allstate Ins. Co.* (2002) 104 CA4th 667, 128 CR2d 358 ("inception of loss" determined not solely by date of physical event causing damage, but also by reference to reasonable discovery of loss).

If the insured has a named-peril policy, rather than an all-risk policy, the principles of inception of the loss set out in *Prudential-LMI Commercial Ins. v Superior Court, supra,* must be applied more broadly. See *Central Nat'l Ins. Co. v Superior Court* (1992) 2 CA4th 926, 3 CR2d 622. In *Central,* the appellate court held that insureds holding a named-peril policy rather than an all-risk policy cannot be deemed to have been on notice of a potentially insured loss unless they had reason to know not only that appreciable damage had occurred but also that the damage was caused by a peril specified in the policy. See also §13.72.

© The Regents of the University of California

§13.95 3. Tolling

If a claim is made and the carrier leads the insured to believe that the claim will be settled, inducing the insured to delay filing suit, the carrier may be estopped from asserting the statute of limitations. *Prudential-LMI Commercial Ins. v Superior Court* (1990) 51 C3d 674, 690, 274 CR 387; *Benner v Industrial Acc. Comm'n* (1945) 26 C2d 346, 350, 159 P2d 24. Under *Prudential-LMI*, the limitations period is tolled while a claim is pending. It ceases to run from the moment the insured gives the carrier formal notice of the claim until the carrier, in writing, denies the claim. See also *Shugerman v Allstate Ins. Co.* (CD Cal 2009) 594 F Supp 2d 1131, 1135 (communication after limitations period expired is not basis for estoppel).

Oral statements denying a claim will not end the tolling period; the carrier must "formally and unequivocally den[y the] claim in writing." *Aliberti v Allstate Ins. Co.* (1999) 74 CA4th 138, 149, 87 CR2d 645.

In *Marselis v Allstate Ins. Co.* (2004) 121 CA4th 122, 16 CR3d 668, the court held that full payment of the claim ends the tolling period, even if the insurer does not provide written notice that the statute of limitations will begin to run on such payment.

Although *Prudential-LMI* ruled on a homeowner's policy, its test for the "inception of the loss" and for tolling the limitations period also applies to commercial property policies. *San Jose Crane & Rigging, Inc. v Lexington Ins. Co.* (1991) 227 CA3d 1314, 1319, 278 CR 301. Finally, *Prudential-LMI* does not operate only prospectively but applies to all claims made before the case was decided. 227 CA3d at 1321.

© The Regents of the University of California

§13.96 4. Action "on the Policy"

If the contractual limitation has run before the insured brings suit, an issue arises whether this fact bars all possible remedies arising from the denial. Insurance Code §2071 applies only to a "suit or action on th[e] policy for the recovery of any claim." Ins C §2071(a). The key phrase is "on the policy." If the suit is not on the policy, the statute of limitations does not bar the action. *Murphy v Allstate Ins. Co.* (1978) 83 CA3d 38, 147 CR 565. Conversely, if the action is on the policy, then all causes of action are apparently barred by the limitation. *Prieto v State Farm Fire & Cas. Co.* (1990) 225 CA3d 1188, 1193, 275 CR 362; *Abari v State Farm Fire & Cas. Co.* (1988) 205 CA3d 530, 536, 252 CR 565. These causes of action can include an action for breach of contract to recover policy benefits, and they may also reach an action for breach of the implied covenant of good faith and fair dealing (see §13.112). *Prieto,* 225 CA3d at 1195.

An action is on the policy if it seeks recovery of policy benefits. Although there is conflict among the cases and the supreme court has yet to address this issue, it appears that if the thrust of the plaintiff's bad faith complaint is to recover policy benefits, the action is "on the policy" and is barred by the contractual limitation, even if phrased in terms of "bad faith." *Prieto v State Farm Fire & Cas. Co., supra*; *Abari v State Farm Fire & Cas. Co., supra*. See also *Jang v State Farm Fire & Cas. Co.* (2000) 80 CA4th 1291, 95 CR2d 917 (action seeking damages under policy framed as bad faith tort claim is subject to contractual limitations period).

Few cases describe what is not an action on the policy. The leading case, *Murphy v Allstate Ins. Co.* (1978) 83 CA3d 38, 147 CR 565, was not merely an action to recover policy benefits. The insureds argued that the carrier had acted wrongfully not only in not paying policy benefits but also by hiring incompetent contractors to repair the insured's home. The court of appeal held that the bad faith cause of action, because it was based on the carrier's responsibility for the contractors' actions, did not come within the statute, because it was not an action on the policy. 83 CA3d at 49. However, *Murphy* also states that the duty of good faith and fair dealing is imposed by law rather than by the policy, and thus an action for its breach is not "on the policy." 83 CA3d at 48. This statement appeared to leave open the possibility that an insured could sue for the *unfair* denial of contract benefits while being precluded from pursuing a straight contractual claim and suffering a defense verdict if unreasonable conduct was *not* proved.

Under one court's analysis, an action will not be on the policy if "the damages [are] not attributable to a risk covered by the policy," even though "the claims arose out of the contractual relationship." *Prieto v State Farm Fire & Cas. Co.* (1990) 225 CA3d 1188, 1193, 275 CR 362. If the insured's damages are not "attributable to a risk covered by the policy," the internal limitation period will not bar the action from compensatory damages for bad faith, a claim for punitive damages, or a claim for emotional distress. *Prieto v State Farm Fire & Cas. Co., supra*; *Murphy v Allstate Ins. Co., supra*.

PRACTICE TIP: Although there is still some uncertainty because the supreme court has not resolved the issue, the court in *Jang v State Farm Fire & Cas. Co., supra,* explained that *Abari v State Farm Fire & Cas. Co., supra,* evinces a trend by the appellate courts to restrict the exemption from the limitations clause set forth in *Murphy v Allstate Ins. Co., supra,* to the facts of that case. The *Jang* court explained that that exemption applies only when the events constituting bad faith occur after initial policy coverage. If denial of the claim in the first instance is the alleged bad faith and the insured seeks policy benefits, the bad faith action is "on the policy" and the limitations provision applies. *Jang v State Farm Fire & Cas. Co.* (2000) 80 CA4th 1291, 1299, 95 CR2d 917. In *Shugerman v Allstate Ins. Co.* (CD Cal 2009) 594 F Supp 2d 1131, 1137 n5, the court recognized the split of authority, and stated that the "more current view is that the one-year statute of limitations applies to bad faith claims where the claim is 'on the policy.'"

© The Regents of the University of California

§13.97 G. Arbitration or Appraisal

The remedy of appraisal to resolve valuation disputes appears to be on the rise. An appraisal constitutes an arbitration (see CCP §§1280-1294.2) and is governed by the same rules that apply to arbitrations. *Devonwood Condominium Owners Ass'n v Farmers Ins. Exch.* (2008) 162 CA4th 1498, 1505, 77 CR3d 88; *Appalachian Ins. Co. v Rivcom Corp.* (1982) 130 CA3d 818, 824, 182 CR 11. If the insured and the carrier cannot agree on the value of a loss, each selects an appraiser to determine that value. Disagreements between the appraisers are resolved by an umpire they select. A majority vote of the three-member appraisal panel fixes the amount of the loss. *Jefferson Ins. Co. v Superior Court* (1970) 3 C3d 398, 400 n2, 90 CR 608.

The appraisal procedure is narrower than conventional arbitrations. Appraisals are designed to fix the amount of a loss, and appraisers cannot, for example, answer questions of policy interpretation or determine whether the insured made any misrepresentations in applying for the policy. See, *e.g., Safeco Ins. Co. v Sharma* (1984) 160 CA3d 1060, 1063, 207 CR 104, which defined the scope of fire appraisal as follows:

> We note, however, one significant difference between the two proceedings. Generally an arbitration proceeding encompasses questions both of fact and of law; hence, "merits of the award, either on questions of law or fact, are generally not subject to review." In contrast, appraisers have the power only to determine a specific question of fact, "namely, the actual cash value of the insured [item]."
>
> As stated in *Hughes v Potomac Ins. Co.* (1962) 199 CA2d 239, 253, 18 CR 650: "The function of appraisers is to determine the amount of damage resulting to various items submitted for their consideration."

See also *Devonwood Condominium Owners Ass'n,* 162 CA4th at 1505.

Although appraisers might also be precluded from determining causation issues, such as whether a covered or an excluded cause is the "predominating" cause of loss, in practice such distinctions are difficult to maintain. When significant causation issues exist, the parties should agree on whether these questions will also be submitted to the panel.

Appraisers selected by the insured and the insurer must be competent and disinterested. Ins C §2071(a). Once an appraisal award is made, it can be confirmed in court as in any arbitration award. *Jefferson Ins. Co. v Superior Court, supra*. However, the appraisers merely determine the loss, *i.e.,* the applicable actual cash value or the replacement cost value, not any liability issues. Therefore, an appraisal award cannot be confirmed as a money judgment in favor of the insured. *Devonwood Condominium Owners Ass'n,* 162 CA4th at 1506.

PRACTICE TIP: Normally, fire appraisal proceedings are quite informal. However, given the finality of this procedure on the question of value, no effort should be spared to carefully define and explain the scope of the appraisers' tasks and to see to it that the issues are fully developed. When necessary, discovery can be obtained through this procedure. See CCP §§1282-1284.3. In appropriate cases, hearings should be stenographically recorded.

© The Regents of the University of California

§13.98 H. California Residential Property Insurance Bill of Rights

As discussed in §13.109, a homeowners' insurer must provide the insured with a California Residential Property Insurance Disclosure form when the policy is issued and each year thereafter. Along with that disclosure form, the insurer must provide the insured with a copy of the California Residential Property Insurance Bill of Rights. Ins C §10103.5(a). This bill of rights begins with a warning that the insured's home and related property is the largest single investment most consumers make. Ins C §10103.5(b). It then sets forth a list of suggestions, including (Ins C §10103.5(b)):

- Read your policy carefully;
- Keep accurate records of improvements to your home;
- Maintain a list of all personal property, pictures, and video equipment, and keep it away from the home;
- Comparison shop for insurance; and
- Determine the cost to rebuild or replace the home.

This bill of rights then sets forth several types of information the insured is entitled to receive from the insurer (Ins C §10103.5(b)):

- The California Residential Property Insurance Disclosure;
- An explanation of how the policy limits were established;
- The insurer's customer service telephone number for underwriting, rating, and claims inquiries;
- An explanation for any cancellation or nonrenewal of the policy;
- A copy of the policy;
- The toll-free telephone number and Internet address for reporting complaints to the Department of Insurance consumer services unit;
- In the event of a claim, an itemized, written scope of loss report prepared by the insurer or its adjuster within a reasonable time period;
- In the event of a claim, notification of a consumer's rights with respect to the appraisal process for resolving claim disputes; and
- In the event of a claim, a copy of the Unfair Practices Act (Bus & P C §§17000-17101) and a copy of the Fair Claims Practices Regulations (10 Cal Code Regs §§2695.1-2695.14).

An insurer of residential property that reports "claims history or loss experience" of insureds to an insurance-supported information database must disclose that fact to the insured. Ins C §10103.5(c)(2).

© The Regents of the University of California

§13.99 IX. HOW IS THE LIABILITY CALCULATED: MEASURE OF INDEMNITY

"Indemnity" in the insurance context means the promise of an insurer to compensate the insured if the insured suffers a loss or damage. *Davis v Phoenix Ins. Co.* (1896) 111 C 409, 43 P 1115. There are two traditional methods of valuing property under property coverages: property that is not repaired or replaced is valued at "actual cash value" (see §13.102); property that is repaired or replaced is valued at "replacement cost value" (see §13.103).

© The Regents of the University of California

A. Policy Limits

§13.100 1. Amount of Coverage

The declarations page for a commercial policy sets forth the policy limits for various types of losses. Different policy limits may be set for structures, personal property, and other coverages. The policy limit will set the maximum that will be paid for that loss. For example, the Building and Personal Property Coverage Form (ISO CP 00 10 04 02) (see §13.38) states: "The most we will pay for loss or damage in any one occurrence is the applicable Limit of Insurance shown in the Declarations." The declarations may not show all the various policy limits, however. For example, the Business and Personal Property Coverage Form (ISO CP 00 10 04 02) contains sections on Additional Coverages and Coverage Extensions, which set forth additional coverages (*e.g.,* debris removal, fire department service charge, pollutant cleanup and removal, increased cost of construction, electronic data, valuable papers and records). These coverages are subject to separate, and relatively low, policy limits (usually ranging from $1000 to $10,000).

NOTE: These additional or extended coverages are often very beneficial to the insured in case of a catastrophic loss. For example, assume the insured's place of business, including the insured's data processing and other computer equipment, was destroyed in a fire. Because there is a separate limit for electronic data processing equipment, the insured does not have to use the business personal property limit to pay for the computer equipment. However, the relatively low limit (usually around $2500) for this equipment will likely be woefully inadequate. Moreover, most insurers contend that the existence of these "additional" or "extended" coverages for electronic data processing equipment precludes recovery of any additional sums for such equipment under the separate business personal property limit. This means that the "additional" and "extended" coverages should be examined closely to make sure the insured is adequately protected.

© The Regents of the University of California

§13.101 2. "Open" Versus "Valued" Policies

An insurance policy is either "open" or "valued." Ins C §410. An open policy is one in which the value of the subject matter is not agreed on, but left open to be ascertained in case of loss. Ins C §411. A valued policy is one that expresses on its face an agreement that the thing insured shall be valued at a specified sum. Ins C §412. Valued policies for property insurance are not common.

Under Ins C §2058, when a valued policy affording fire coverage is issued and a fire loss occurs, if the insured repairs or replaces the property the insured receives full payment for the loss up to the face amount of the policy; if the property is not repaired or replaced, the insured receives either the replacement value of the loss or the face amount of the policy, whichever is less.

© The Regents of the University of California

§13.102 B. Actual Cash Value

Actual cash value (ACV) is defined in Ins C §2051(b) as follows:

> (1) In case of total loss to the structure, the policy limit or the fair market value of the structure, whichever is less;
> (2) In case of a partial loss to the structure, or loss to its contents, the amount it would cost the insured to repair, rebuild or replace the thing lost or injured less a fair and reasonable deduction for physical depreciation based upon its condition at the time of the injury or the policy limit, whichever is less. In case of partial loss to the structure, a deduction for physical depreciation shall apply only to components of a structure that are normally subject to repair and replacement during the useful life of that structure.

Before the codification of this definition, courts enforced different definitions of ACV. For example, in *Cheeks v California Fair Plan Ass'n* (1998) 61 CA4th 423, 429 n5, 71 CR2d 568, the policy defined ACV to mean "actual cash value, with proper deduction for depreciation." In *Community Assisting Recovery, Inc. v Aegis Sec. Ins. Co.* (2001) 92 CA4th 886, 893, 112 CR2d 304, the court held that ACV was not the exclusive standard, and insurers could use market value, replacement cost, cost of repair, or replacement cost less depreciation.

NOTE: Now that the legislature has defined ACV, it remains to be seen whether different standards or different definitions of ACV will be enforceable.

In *Everett v State Farm Gen. Ins. Co.* (2008) 162 CA4th 649, 658, 75 CR3d 812, the court noted that ACV "oftentimes is insufficient to repair or replace the property," and that replacement cost coverage "is intended to compensate the insured for the shortfall in coverage that results from rebuilding under a policy that pays only for actual cash value."

© The Regents of the University of California

§13.103 C. Replacement Cost Value

Replacement cost value (RCV) means the cost to repair or replace the damaged or destroyed property, with like or equivalent construction, without deduction for depreciation. See Ins C §§2051.5, 10102. Replacement cost value is intended to compensate the insured for the shortfall in coverage that may result from rebuilding if the policy only provided for actual cash value (ACV) (see §13.102). *Everett v State Farm Gen. Ins. Co.* (2008) 162 CA4th 649, 658, 75 CR3d 812; *Fire Ins. Exch. v Superior Court* (2004) 116 CA4th 446, 462, 10 CR3d 617. Replacement cost value necessarily places the insured in a better position than actual cash value would provide. 116 CA4th at 464.

In the replacement of a structure, replacement cost value must be the cost to replace it at the same site. However, case law has established that the insured can purchase an existing, comparable structure, or build at a different site, as long as the cost does not exceed what it would have cost to rebuild at the original site. *Conway v Farmers Home Mut. Ins. Co.* (1994) 26 CA4th 1185, 1188, 31 CR2d 883. If the insured finds a bargain property, the insured cannot recover a windfall; the maximum the insured can recover is the amount actually expended. 26 CA4th at 1190. This case law is now codified in Ins C §2051.5(c), which states that no homeowners' policy may limit or deny payment of RCV in the event the insured decides to rebuild or replace the property at a location other than the insured premises. The replacement cost, however, shall be calculated on the basis of the cost to rebuild at the original site.

Some commercial property policies impose a time limit within which the property must be repaired or replaced in order for the insured to recover RCV. For example, the ISO Businessowners Special Property Coverage Form (BP 00 02 12 99) and the ISO Homeowners 3 Coverage Form (HO 00 03 10 90) (see §13.35) contain such a provision, although the ISO Building and Personal Property Coverage Form (CP 00 10 04 02) does not. Such a provision typically gives the insurer the right to pay the ACV and withhold the difference between the ACV and the RCV until completion of repairs. Completion of repairs, or purchase of a substitute property, is considered a condition precedent to receiving RCV. See *Fraley v Allstate Ins. Co.* (2000) 81 CA4th 1282, 1287, 97 CR2d 386. However, some insurers will agree to make progress payments as the repairs reach certain degrees of completion.

A homeowners' insurer must pay the actual cash value, until the damaged property is repaired, rebuilt, or replaced. Ins C §2051.5(a). A homeowners' policy must allow the insured at least 12 months from the date the first ACV payment is made to collect the full RCV. An insured may obtain an extension of 6 months for "good cause."

In *City of Hollister v Monterey Ins. Co.* (2008) 165 CA4th 455, 81 CR3d 72, after a fire damaged a building insured under a commercial property policy, the insured city sought to recover the building's "functional replacement value." To recover such benefits, the policy required the city to enter into a contract to repair or replace the building within 180 days after the fire. The court held that, even though the 180-day replacement provision was a condition precedent, the insurer was equitably estopped to assert the provision because it failed to cooperate with and assist the city in determining the extent of the insured's additional liability and actively interfered with performance of the city's contracting condition by obstructing, delaying, and interfering with the city's efforts to determine its rights under the policy. 165 CA4th at 491.

© The Regents of the University of California

§13.104 D. Guaranteed Replacement Cost

Guaranteed replacement cost coverage requires the insurer, in the event of a loss, to pay the full amount needed to repair or replace the damaged or destroyed property with like or equivalent construction regardless of the stated policy limit. See Ins C §10102. In addition, an insured can elect to purchase this coverage with full building code upgrade coverage or with limited building code upgrade coverage, under which the insurer pays the additional costs of repairing or replacing the damaged structure to comply with any new building standards, such as building codes or zoning laws required by government agencies and in effect at the time of rebuilding.

NOTE: The policy must specify whether the insured must "actually repair or replace the damaged or destroyed dwelling in order to recover guaranteed replacement cost." Ins C §10102(a).

See Ins C §10102 regarding the California Residential Property Insurance Disclosure. See §13.109.

© The Regents of the University of California

§13.105 E. Extended Replacement Cost

Extended replacement cost coverage requires the insurer, in the event of a loss, to pay to repair or replace the damaged or destroyed structure with like or equivalent construction up to a specified percentage over the stated policy limit. This percentage is often 125 percent.

In *Major v Western Home Ins. Co.* (2009) 169 CA4th 1197, 87 CR3d 556, the policy (1) provided extended replacement cost benefits up to 25 percent over the stated policy limit for the dwelling and (2) required that the dwelling coverage limit be equal to the cost to replace the home to be determined by a home inspection. The inspection revealed that the dwelling coverage limit was lower than the cost to replace the home. Raising the dwelling limit would have resulted in an increase in the limit applicable to personal property, which was a percentage of the dwelling limit. The insurer failed to raise the coverage limits until after a fire destroyed the home, and then argued it was done as a "courtesy." The appellate court rejected the argument, held the insurer had been contractually bound to increase the personal property limits, and affirmed the jury's finding that the insurer acted in bad faith.

© The Regents of the University of California

§13.106 F. Inflation Guard

Some policies offer additional protection against increases in repair or replacement costs that reflect increased costs of building materials or labor. This feature may have different names, but often is called "inflation guard." When this option is selected, the insurer will automatically increase the policy limit on renewal. However, the insured should still make sure that the limit is adequate and should notify the agent or broker of any additions or modifications to the structure that would increase its value faster than the general inflation rate.

In *Everett v State Farm Gen. Ins. Co.* (2008) 162 CA4th 649, 661, 75 CR3d 812, the insured received a California Residential Property Insurance Disclosure statement, which provided that, to be eligible for extended replacement cost coverage, the insured must insure the property to its full replacement cost at the time the policy is issued with possible periodic adjustments for inflation. The insurer sent annual renewal certificates reminding the insured that the stated replacement cost figure was merely an estimate, and it was the insured's responsibility to determine whether the property was adequately insured. The court held that it was the insured's duty to determine whether the coverage was sufficient and that an inflation coverage provision did not lead the insured to believe that the policy provided for 100-percent replacement cost. 162 CA4th at 661.

© The Regents of the University of California

§13.107 G. Code-Mandated Repairs

Although the concept of "replacement cost" (*i.e.,* new for old) is now universally accepted (see §13.103), a significant but perhaps not completely resolved issue is coverage for code-mandated techniques or materials that increase the cost of repair or replacement of a damaged structure.

Courts have held that an insurer is not obligated to pay for code-mandated changes in construction (see *McCorkle v State Farm Ins. Co.* (1990) 221 CA3d 610, 270 CR 492), even when the insured's policy states that the carrier will pay the full cost to repair or replace without regard to policy limits (see *Bischel v Fire Ins. Exch.* (1991) 1 CA4th 1168, 2 CR2d 575). In both of these cases, the courts looked to Ins C §§2070-2071, but did not address the fact that the basic fire insurance policy set forth in §2071 is a traditional indemnity contract; superior levels of coverage can be provided (Ins C §2070), and an insurer is free to enhance benefits or delete clauses that impose duties or limitations on an insured. Ins C §2079.

Given the importance of this issue, it should be expected that insureds will challenge this limitation on the following bases:

- Representations in brochures, advertising, or at the point of sale (*Dobosz v State Farm Fire & Cas. Co.* (Ill Ct App 1983) 458 NE2d 611; *Jones v Crown Life Ins. Co.* (1978) 86 CA3d 630, 150 CR 375 (obligation to inform insured of policy exclusions); *Bass v John Hancock Mut. Life Ins. Co.* (1974) 10 C3d 792, 112 CR 195 (insurer could not rely on employee's prior rejection of employer's group plan after terms were changed); *Laing v Occidental Life Ins. Co*. (1966) 244 CA2d 811, 53 CR 681 (insured entitled to rely on insurer's representations even though insured failed to read policy); but see *Brown v Royal Maccabees Life Ins. Co.* (10th Cir 1998) 137 F3d 1236 (insured could not rely on insurer's computer-generated false illustration of insured's actuarial situation, resulting from programming error, that was at variance with policy terms));
- Waiver or estoppel theories (*Ivey v United Nat'l Indem. Co.* (9th Cir 1958) 259 F2d 205 (estoppel based on insurer's representations)); or
- The theory that the limitation was not brought to the insured's attention (see generally *State Farm Mut. Auto. Ins. Co. v Jacober* (1973) 10 C3d 193, 110 CR 1; *Logan v John Hancock Mut. Life Ins. Co.* (1974) 41 CA3d 988, 116 CR 528).

In an apparent attempt to clarify whether a policy covers code-mandated changes, the legislature enacted Ins C §§10101-10107. Section 10101 requires the insurer to give a copy of the California Residential Property Insurance Disclosure Statement (set forth in Ins C §10102; see §13.109) to the named insured on the application, or the initial renewal, of any residential property insurance policy. The disclosure statement describes the principal forms of residential insurance coverage available in California. The insurer must identify on the disclosure form the type of coverage purchased or selected. The form indicates, among other matters, whether the coverage includes building code upgrades.

The issue of code-mandated repairs overlaps with the law and ordinance exclusion found in most policies. In *Bischel v Fire Ins. Exch., supra,* the court held in favor of the insurer, not only because the insured was entitled under the policy to have his dock restored only to its former condition, but also because the extra expense was mandated by government regulation, bringing the claim within the law and ordinance exclusion. *Bischel,* 1 CA4th at 1173. See §13.87 on law and ordinance exclusions.

© The Regents of the University of California

§13.108 H. Deductibles

A "deductible" is the amount of loss the insured absorbs before the carrier's duty to indemnify is triggered. Deductibles vary widely by line and product. The greater the amount of risk an insured can accept in deductibles, the lower the insured's premium. Because modest increases in the deductible often result in surprisingly large reductions in the premium, insurance purchasers should always obtain quotes for a wide variety of deductibles.

© The Regents of the University of California

§13.109 I. Additional Requirements for Homeowners' Policies

The declarations page for a homeowners' policy must set forth the limit of coverage for the structure and state that the limit is based on an estimate of the cost to rebuild the home, including an approximate cost for labor and materials. Ins C §10103(a)(2). If the policy does not provide coverage for building code upgrades (see below), the declarations page must contain a statement to that effect. Ins C §10103(a)(5).

In addition, a homeowners' insurer must provide a California Residential Property Insurance Disclosure form when a homeowners' policy is issued and each year thereafter while the policy remains in force. Ins C §10101. The disclosure statement must indicate which of the following categories of insurance the insured has selected (Ins C §10102):

- Guaranteed Replacement Cost Coverage With Full Building Code Upgrade, which pays replacement costs without regard to policy limits, and includes costs resulting from code changes;
- Guaranteed Replacement Cost Coverage With Limited or No Building Code Upgrade, which pays replacement costs without regard to policy limits, but limits or excludes costs resulting from code changes;
- Extended Replacement Cost, which pays replacement costs up to a specified percentage above the policy limit;
- Replacement Cost, which pays replacement costs up to the stated policy limit;
- Actual Cash Value, which pays the fair market value of the structure at the time of the loss, up to the stated policy limit; or
- Building Code Upgrade—Ordinance or Law Coverage, which pays, up to limits specified in the policy, additional costs required to bring the dwelling up to code.

Homeowners' insurance may not be labeled as "Guaranteed Replacement Cost Coverage" if it specifies maximum coverage amounts in terms of set dollar limits, percentage amounts, construction cost limits, indexing, or any other preset maximum for covered damage to the insured dwelling. Ins C §10102(e).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.110 J. Coinsurance Clauses

§13.110 J. Coinsurance Clauses

Coinsurance encourages a client to carry adequate coverage and to pay adequate premiums to the insurer. Typically, an insured is required to carry an amount of insurance equal to a certain percentage of the replacement cost of the insured property, usually 80 to 90 percent. In exchange, the carrier agrees to pay 100 percent of all partial losses up to the value of the policy, less the deductible. An insured who fails to maintain an adequate insurance-to-value ratio may face a "coinsurance penalty" after a partial loss and receive less than the full replacement cost of the damaged property. *Los Angeles Mut. Ins. Co. v Cawog* (1973) 30 CA3d 378, 385, 106 CR 307.

© The Regents of the University of California

§13.111 K. Value Reporting Clauses Regarding Inventory

Business property policies often require the insured to report inventories and property values on some type of periodic basis. The value of the inventory or property listed in the report may cause the insurer to assess an additional premium.

Under the ISO Value Reporting Form (CP 13 10 04 02), the insurer may require reports on a daily, weekly, monthly, or quarterly basis. This form adds a coinsurance condition that provides that if the insured's most recent report of values before the loss shows less than the full value of the covered property at that location on the report date, the insurer will pay only a proportion of the loss payable. The proportion is the ratio of value reported to the actual value of the covered property on the report date.

In addition, this form contains a "Failure to Submit Reports" condition that also limits the amounts the insurer will pay. This condition states:

> If at the time of loss or damage you have failed to submit the following:
> a. The first required report of values:
> (1) We will not pay more than 75 percent of the amount we would otherwise have paid; and
> (2) We will pay only for loss or damage at locations shown in the declarations.
> b. Any required report of values after the first required report:
> (1) We will not pay more for loss or damage at any location than the values you last reported for that location; and
> (2) We will pay only for loss or damage at locations reported in your last report filed before the loss.

© The Regents of the University of California

X. WHEN THINGS GO WRONG: CLAIMS AGAINST THE INSURER

§13.112 A. Common Law Bad Faith

The duty of good faith and fair dealing requires that neither party to the contract do anything to deprive the other of benefits due under the contract. *Egan v Mutual of Omaha Ins. Co.* (1979) 24 C3d 809, 818, 169 CR 691. The covenant of good faith is a supplement to the express contractual agreements and does not exist separately from its contractual underpinnings. *McMillin Scripps North v Royal Ins. Co.* (1993) 19 CA4th 1215, 1222, 23 CR2d 243.Thus, if no breach of contract can be shown, there is no basis for finding a breach of the covenant of good faith. *Kransco v American Empire Surplus Lines Ins. Co.* (2000) 23 C4th 390, 408, 97 CR2d 151; *Waller v Truck Ins. Exch.* (1995) 11 C4th 1, 35, 44 CR2d 370; *San Diego Housing Comm'n v Industrial Indem. Co.* (1998) 68 CA4th 526, 544, 80 CR2d 393.

The gravamen of a claim for first party bad faith is the insurer's refusal, without proper cause, to compensate the insured for a loss covered by the policy, or the insurer's unreasonable delay in paying benefits due under the policy. *Gruenberg v Aetna Ins. Co.* (1973) 9 C3d 566, 574, 108 CR 480; *Waters v United Servs. Auto. Ass'n* (1996) 41 CA4th 1063, 1070, 48 CR2d 910; *Austero v National Cas. Co.* (1978) 84 CA3d 1, 29, 148 CR 653, disapproved on other grounds in *Egan v Mutual of Omaha Ins. Co*. (1979) 24 C3d 809, 169 CR 691. Mere denial of benefits is not bad faith by itself. *Dalrymple v United Servs. Auto. Ass'n* (1995) 40 CA4th 497, 523, 46 CR2d 845; *Opsal v United Servs. Auto. Ass'n* (1991) 2 CA4th 1197, 1205, 10 CR2d 352; *Safeco Ins. Co. v Guyton* (9th Cir 1982) 692 F2d 551, 557. A denial of coverage based on a reasonable, but incorrect, interpretation of the insurance policy will ordinarily not support a bad faith action. *Dalrymple v United Servs. Auto. Ass'n, supra*; *Opsal v United Servs. Auto. Ass'n, supra*; *Hanson v Prudential Ins. Co.* (9th Cir 1985) 772 F2d 580.

Two recent cases disagree whether subjective bad faith plays a part if an insurer defends against a bad faith claim under the genuine dispute doctrine. In *Brehm v 21st Century Ins. Co.* (2008) 166 CA4th 1225, 83 CR3d 410, the insured sued the insurer for bad faith failure to settle prior to arbitration. The insurer demurred, arguing the dispute presented "a classic 'genuine dispute' as to the value of the insured's claim," because the insurer relied on an expert to evaluate the insured's claim. The trial court sustained the insurer's demurrer without leave to amend. The appellate court reversed, holding that the insurer could not prevail without showing both objectively reasonable conduct and good faith subjective intent.

In contrast, in *Bosetti v U.S. Life Ins. Co. in City of New York* (2009) 175 CA4th 1208, 1236, 96 CR3d 744, the appellate court held that "good faith" is an objective standard. "Not only is subjective bad faith unnecessary to establish a bad faith cause of action, it is also insufficient to do so." 175 CA4th at 1236. To support this conclusion, the *Bosetti* court relied on *Carma Developers (Cal.), Inc. v Marathon Dev. Cal., Inc.* (1992) 2 C4th 342, 373, 6 CR2d 467, in which the supreme court held that "the covenant of good faith can be breached for objectively unreasonable conduct, regardless of the actor's motive." See *Bosetti*, 175 CA4th at 1236. The *Bosetti* court expressly disagreed with *Brehm* to the extent *Brehm* held there is a distinct subjective good faith requirement. *Bosetti*, 175 CA4th at 1238.

Generally, bad faith cannot exist in the absence of coverage. In certain circumstances, however, California courts have held that even a claim that does not come within a policy's coverage may trigger a bad faith claim if unreasonable failure to investigate the claim, or unreasonable delay in providing a coverage decision, harms an insured. Further, if the carrier provides a defense in liability litigation, it can incur bad faith liability by mishandling that defense, even if a court later finds that it owed no duty to defend. See *Travelers Ins. Co. v Lesher* (1986) 187 CA3d 169, 186, 231 CR 791, disapproved on other grounds in *Buss v Superior Court* (1997) 16 C4th 35, 50 n12, 65 CR2d 366. But see *Shade Foods, Inc. v Innovative Prods. Sales & Mktg., Inc.* (2000) 78 CA4th 847, 886, 93 CR2d 364 (court affirmed insurer's bad faith failure "to conduct a meaningful investigation before denying coverage," but reversed large punitive damages award because insurer's conduct was not proved "despicable" by clear and convincing evidence as required by CC §3294).

In sum, the reasonableness of the carrier's conduct in adjusting and paying, or in denying, a claim rests on three considerations:

- Was its decision to deny the claim based on an adequate and thorough investigation? See *Egan v Mutual of Omaha Ins. Co.* (1979) 24 C3d 809, 819, 169 CR 691. But see *Jordan v Allstate Ins. Co.* (2007) 148 CA4th 1062, 56 CR3d 312 *(Jordan II)* (insurer failed to conduct a "full, fair, thorough and timely" investigation of the alleged collapse, but bad faith claim requires insured to prove coverage); *Benavides v State Farm Gen. Ins. Co.* (2006) 136 CA4th 1241, 1250, 39 CR3d 650 (if insurer's investigation, adequate or not, results in correct conclusion of no coverage, no tort liability arises for breach of covenant of good faith).
- Did the carrier delay unreasonably in deciding either to pay or to deny the claim? See *McCormick v Sentinel Life Ins. Co.* (1984) 153 CA3d 1030, 1049, 200 CR 732.
- Was the carrier's decision to withhold coverage a reasonable interpretation of the policy in light of the facts the carrier knew or should have known? See *Hanson v Prudential Ins. Co., supra*.

© The Regents of the University of California

§13.113 B. Damages

Breach of the insurance contract, without bad faith, will support an award of contract benefits. Prejudgment interest may be recoverable if the amount due was certain or capable of being made certain by calculation. CC §3287(a); *Fireman's Fund Ins. Co. v Allstate Ins. Co.* (1991) 234 CA3d 1154, 1173, 286 CR 146.

An insured who establishes bad faith may recover a full array of tort remedies, including those described in §§13.114-117.

© The Regents of the University of California

§13.114 1. Emotional Distress

Proximate cause is required for recovery of emotional distress damages in bad faith cases. *Major v Western Home Ins. Co.* (2009) 169 CA4th 1197, 1215, 87 CR3d 556. Claims of emotional distress must be incidental to "a substantial invasion of property interests." *Gourley v State Farm Mut. Auto. Ins. Co.* (1991) 53 C3d 121, 128, 3 CR2d 666; *Major,* 169 CA4th at 1214. Therefore, emotional distress damages must be tied to actual, not merely potential, economic loss. *Continental Ins. Co. v Superior Court* (1995) 37 CA4th 69, 85, 43 CR2d 374; *Major,* 169 CA4th at 1214.

Although unreasonable delay in paying benefits is actionable as bad faith, "a delay in paying policy benefits, even if in an unreasonable manner, does not in itself establish economic loss to the plaintiff" so as to justify emotional distress damages. *Maxwell v Fire Ins. Exch.* (1998) 60 CA4th 1446, 1450; 70 CR2d 866; *Major,* 169 CA4th at 1214. On the other hand, the requirement of economic loss for recovery of emotional distress damages may be satisfied by the insured's payment of legal fees and court costs to enforce the claim under the policy. *Delos v Farmers Group, Inc.*, (1979) 93 CA3d 642, 659, 155 CR 843; *Major,* 169 CA4th at 1214.

© The Regents of the University of California

§13.115 2. Attorney Fees and Costs

The insured may obtain attorney fees and costs incurred for recovery of wrongfully withheld policy benefits (known as *Brandt* fees), but not fees or costs incurred in proving tort claims. See *Brandt v Superior Court* (1985) 37 C3d 813, 817, 210 CR 211; *Slottow v American Cas. Co*. (9th Cir 1993) 10 F3d 1355, 1362 (applying California law, holding it is insured's burden to allocate fees and costs incurred to recover policy benefits). See also *Essex Ins. Co. v Five Star Dye House, Inc.* (2006) 38 C4th 1252, 45 CR3d 362 (assignee of bad faith claim for insurer's wrongful withholding of policy benefits may recover *Brandt* fees); CACI 2350 (plaintiff "may recover attorney fees… incurred to obtain policy benefits but not attorney fees… incurred for other purposes"). Courts have reached conflicting results on whether attorney fees incurred in defending against an insurer's unsuccessful appeal are recoverable. See *Baron v Fire Ins. Exchange* (2007) 154 CA4th 1184, 1198, 65 CR3d 502 (allowing recovery of fees on appeal); *Track Mortgage Group, Inc. v Crusader Ins. Co.* (2002) 98 CA4th 857, 120 CR2d 228 (allowing recovery of fees on appeal); *Shade Foods, Inc. v Innovative Prods. Sales & Mktg., Inc.* (2000) 78 CA4th 847, 93 CR2d 364 (fees on appeal not recoverable); *Burnaby v Standard Fire Ins. Co.* (1995) 40 CA4th 787, 47 CR2d 326 (fees on appeal not recoverable); *McGregor v Paul Revere Life Ins. Co.* (9th Cir 2004) 369 F3d 1099, 1101 (predicting the California Supreme Court will allow recovery of fees on appeal). See also *Textron Fin. Corp. v National Union Fire Ins. Co.* (2004) 118 CA4th 1061, 1075, 13 CR3d 586 (when insured had contingency fee agreement, insured's attorney fee recovery was limited to amount specified by contract; insured cannot seek "reasonable value" of fees in excess of amount set by contract).

If the insured has a contingency fee agreement with its attorneys, the trier of fact must determine the percentage of the legal fees paid to the attorney that reflects the work attributable to obtaining the contract recovery. In *Cassim v Allstate Ins. Co*. (2004) 33 C4th 780, 16 CR3d 374, the California Supreme Court set out the following method of calculation (33 C4th at 812):

> To determine the percentage of the legal fees attributable to the contract recovery, the trial court should determine the total number of hours an attorney spent on the case and then determine how many hours were spent working exclusively on the contract recovery. Hours spent working on issues jointly related to both the tort and contract should be apportioned, with some hours assigned to the contract and some to the tort. This latter figure, added to the hours spent on the contract alone, when divided by the total number of hours worked, should provide the appropriate percentage.

The court further held that no portion of legal fees attributable to the punitive damage award can be recovered as *Brandt* fees and that *Brandt* fees can never exceed the legal fees for the combined tort and contract recovery (in most cases, the court noted, the amount will be far less). 33 C4th at 812.

The court also held that the insured bears the burden of proof to demonstrate how fees for work attributable to both the tort and contract recoveries should be apportioned. Trial courts have discretion to disregard fee arrangements that appear to be designed to manipulate the calculation of *Brandt* fees for the insured's benefit. 33 C4th at 813. In *Major v Western Home Ins. Co.* (2009) 169 CA4th 1197, 1218, 87 CR3d 556, the court described the type of testimony that supported plaintiffs' claim for *Brandt* fees:

> [C]ounsel for the Majors testified in detail about the amount of fees the Majors incurred. He testified that he reviewed the entire file, carefully allocated the time devoted to the prosecution of the complaint against Western, broke out the time devoted to the contract portion of the complaint, and the time that could not be segregated. He identified and requested hourly billing rates lower than the rates a court had awarded in a recent insurance bad faith case, and stated he had not billed for at least 200 hours in trial preparation and for the trial itself. He also described the costs incurred in connection with the action and reduced that amount by nearly half to account for those costs attributable to the prosecution of the contract action only.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.116 3. Consequential Economic Loss

§13.116 3. Consequential Economic Loss

The insured may also recover consequential economic losses, such as loss of property in a foreclosure or forced sale (*Little v Stuyvesant Life Ins. Co*. (1977) 67 CA3d 451, 465 n3, 136 CR 653; *Merlo v Standard Life & Acc. Ins. Co*. (1976) 59 CA3d 5, 16, 130 CR 416); loss of future earnings and profits (*Gruenberg v Aetna Ins. Co.* (1973) 9 C3d 566, 580, 108 CR 480); or costs of borrowing to preserve assets or meet living expenses (*Little v Stuyvesant Life Ins. Co., supra*).

© The Regents of the University of California

4. Punitive Damages

§13.117 a. Clear and Convincing Evidentiary Standard

If the jury finds, by clear and convincing evidence, that the insurer acted with "oppression, fraud, or malice," the insured may recover punitive damages. See CC §3294; *Jordan v Allstate Ins. Co.* (2007) 148 CA4th 1062, 1080, 56 CR3d 312 *(Jordan II)*; *Hangarter v Provident Life & Acc. Ins. Co.* (9th Cir 2004) 373 F3d 998. For example, in *Diamond Woodworks, Inc. v Argonaut Ins. Co.* (2003) 109 CA4th 1020, 1050, 135 CR2d 736, the court held that punitive damages were supported by the insurer's

> near reflexive denial of the severely maimed [employee's] employment status and entitlement to workers' compensation benefits, not to mention their subsequent long-term refusal to budge from that position, [and the fact that] the evidence was consistent with intentional fraud, and not consistent with mistake, honest error, negligence….

Although the same evidence used to establish bad faith may be used to establish oppression, fraud, or malice, the higher standard of clear and convincing evidence is required to impose punitive damages. Thus, a "marginally sufficient case of bad faith is not likely to prove malice or oppression by clear and convincing evidence." *Shade Foods, Inc. v Innovative Prods. Sales & Mktg., Inc*. (2000) 78 CA4th 847, 909, 93 CR2d 364. Punitive damages are appropriate "when tortious conduct rises to levels of extreme indifference to the plaintiff's rights, a level which decent citizens should not have to tolerate." *Food Pro Int'l, Inc. v Farmers Ins. Exchange* (2008) 169 CA4th 976, 994, 89 CR3d 1, quoting *American Airlines, Inc. v Sheppard, Mullin, Richter & Hampton* (2002) 96 CA4th 1017, 1051, 117 CR2d 685. However, punitive damages should not be allowed when the offending conduct is consistent with "a mistake of law or fact, honest error of judgment, overzealousness, mere negligence or other such noniniquitous human failing." *Food Pro*, 169 CA4th at 994, quoting *Tomaselli v Transamerica Ins. Co.* (1994) 25 CA4th 1269, 1288 n14, 31 CR2d 433. See also *Patrick v Maryland Cas. Co*. (1990) 217 CA3d 1566, 1576, 267 CR 24 (claims handling that is "witless and infected with symptoms of bureaucratic inertia and inefficiency" does not add up to malice or oppression).

NOTE: An insured's egregious misconduct may justify punitive damages, but that liability may not be shifted to the insurer; only an insurance company's own egregious misconduct may justify an award of punitive damages. See *PPG Indus., Inc. v Transamerica Ins. Co*. (1999) 20 C4th 310, 84 CR2d 455.

© The Regents of the University of California

§13.117A b. "Clear and Convincing" Evidence Is Required for Punitive Damages

The "clear and convincing" evidentiary standard also applies to summary judgment or summary adjudication motions (see *Food Pro Int'l, Inc. v Farmers Ins. Exchange* (2008) 169 CA4th 976, 994, 89 CR3d 1; *Basich v Allstate Ins. Co.* (2001) 87 CA4th 1112, 1118, 105 CR2d 153), and to motions for nonsuit, challenging punitive damage claims (see *Stewart v Truck Ins. Exch.* (1993) 17 CA4th 468, 21 CR2d 338). The judge must "view the evidence presented through the prism of the substantive [clear and convincing] evidentiary burden." *Anderson v Liberty Lobby, Inc.* (1986) 477 US 242, 254, 106 SC 2505, 91 L Ed 2d 202, as quoted in *Food Pro Int'l*, 169 CA4th at 994.

© The Regents of the University of California

§13.117B c. Corporate Entities May Be Held Liable for Punitive Damages Based on the Acts or Omissions of a "Managing Agent"

California follows the rule of Restatement (Second) of Torts §909 (Tent. Draft No. 19, 1973) that a corporation may be held liable for punitive damages for the acts of an agent employed in a "managerial capacity." *Egan v Mutual of Omaha Ins. Co.* (1979) 24 C3d 809, 822, 169 CR 691. The determination whether employees act in a managerial capacity does not hinge on their "level" in the corporate hierarchy, but rather on the degree of discretion the employee possesses in making corporate policy. In the context of insurance claims, the Court held (24 C3d at 823):

> When employees dispose of insureds' claims with little if any supervision, they possess sufficient discretion for the law to impute their actions concerning those claims to the corporation.

The employees were "managerial employees" because they exercised broad discretion in disposing of the plaintiff's claim.

The year after *Egan* was decided, the Legislature amended CC §3294(b) to require a plaintiff to prove that an officer, director, or managing agent of the defendant authorized or ratified the wrongful conduct for which the damages are awarded in order to obtain punitive damages against a corporate defendant. Such authorization or ratification must be proved by clear and convincing evidence. *Barton v Alexander Hamilton Life Ins. Co.* (2003) 110 CA4th 1640, 1644, 3 CR3d 258; CACI 3943.

Insurers have argued that use of the term "managing agent" rather than "managerial employee" in amended CC §3294(b) eliminated *Egan*'s holding that punitive damages could be imposed on an insurer for the acts of claims personnel, even though *White v Ultramar, Inc.* (1999) 21 C4th 563, 88 CR2d 19 established that the 1980 amendments to §3294 did not alter *Egan*'s definition of "managing agent." In *Major v Western Home Ins. Co.* (2009) 169 CA4th 1197, 87 CR3d 556, the appellate court held that a claims person who managed an office without day-to-day oversight, supervised lower ranking employees, supervised the handling of claims, and authorized payment of benefits was a "managing agent" of the insurer, even though employed by a separate company. 169 CA4th at 1221. See *Textron Financial Corp. v National Union Fire Ins. Co.* (2004) 118 CA4th 1061, 1080, 13 CR3d 586 (third party insurance agency was "managing agent" of insurer, because agency could independently solicit, bind, write, and administer liability policies; participated in issuing, canceling, and reinstating policies; and advised and participated in ultimate decision to deny claim); *Hergenroeder v Travelers Prop. & Cas. Co.* (ED Cal 2008) 249 FRD 595, 620 (claims person with only $60,000 in claims handling authority was not "managing agent" as to claim for over $300,000 in policy benefits).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.118 d. Constitutionality of Punitive Damages

§13.118 d. Constitutionality of Punitive Damages

Under California law, a punitive damage award must be based on three factors: (1) the reprehensibility of the defendant's conduct; (2) the amount of compensatory damages awarded to or actual harm suffered by the plaintiff; and (3) the defendant's financial condition. *Adams v Murakami* (1991) 54 C3d 105, 110, 284 CR 318, 320; *Neal v Farmers Ins. Exchange* (1978) 21 C3d 910, 928, 148 CR 389, 399. Federal cases have shifted the focus to the constitutionality of punitive damage awards under federal due process standards. In *State Farm Mut. Auto. Ins. Co. v Campbell* (2003) 538 US 408, 155 L Ed 2d 585, 123 S Ct 1513, the United States Supreme Court held that the due process clause of the Fourteenth Amendment prohibits grossly excessive or arbitrary punishment of a tortfeasor, and therefore limits the amount of punitive damages that a state court may award. The *State Farm Court* required courts reviewing a punitive damages award to evaluate whether the award of punitive damages was excessive in light of the following "guideposts":

- The degree of reprehensibility of the defendant's conduct (see §13.118A);
- The disparity between the actual or potential harm suffered by the plaintiff and the punitive damages awarded (see §13.118B); and
- The difference between the punitive damages awarded by the jury and the penalties authorized or imposed in comparable cases (see §13.118C).

The first two guideposts are appropriate for a jury to consider in determining the amount of a punitive damages award; the third guidepost is an appropriate consideration only for a reviewing court. *Bullock v Philip Morris USA, Inc.* (2008) 159 CA4th 655, 689, 71 CR3d 775; *Century Sur. Co. v Polisso* (2006) 139 CA4th 922, 959, 43 CR3d 468.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.118A (1) First Guidepost: Reprehensibility of Defendant's Conduct

§13.118A (1) First Guidepost: Reprehensibility of Defendant's Conduct

State Farm Mut. Auto. Ins. Co. v Campbell (2003) 538 US 408, 419; 155 L Ed 2d 585, 602; 123 S Ct 1513 explained that reprehensibility of the defendant's conduct is the "most important indicium of the reasonableness of a punitive damage award." See also *BMW of N. Am. v Gore* (1996) 517 US 559, 575; 116 S Ct 1589, 1599, 134 L Ed 2d 809. The issue of reprehensibility requires the court to examine whether:

- The harm caused was physical as opposed to economic;
- The tortious conduct evinced an indifference to or a reckless disregard of the health or safety of others;
- The target of the conduct had financial vulnerability;
- The conduct involved repeated actions or was an isolated incident; and
- The harm was the result of intentional malice, trickery, deceit, or mere accident.

Repeated misconduct is more reprehensible than an individual act of malfeasance. *State Farm*, 538 US at 423; *Johnson v Ford Motor Co.* (2005) 35 C4th 1191, 1202, 29 CR3d 401. Similar conduct need not be identical, but courts must ensure that it constitutes replication of the prior transgressions. *Johnson,* 35 C4th at 1204. Evidence of wide-ranging, dissimilar business practices may not be used to show reprehensibility, because a "defendant should be punished for the conduct that harmed the plaintiff, not for being an unsavory individual or business." *State Farm*, 538 US 408, 421. However, a refusal to defend an insured may be considered more than a single event, if it consists of a series of acts or course of conduct committed over a period of time. *Century Sur. Co. v Polisso* (2006) 139 CA4th 922, 965, 43 CR3d 468.

A jury may consider evidence of harm to others in determining the degree of reprehensibility of the defendant's conduct, but may not award punitive damages for the purpose of punishing a defendant for harm caused to nonparties to the litigation. *Philip Morris USA v Williams* (2007) 549 US 346, 355, 166 L Ed 2d 940, 949, 127 S Ct 1057. Evidence of harm to nonparties may be admitted for the limited purpose of determining reprehensibility, but may not be used for the purpose of determining the amount of punitive damages. For this reason, in *Bullock v Philip Morris USA, Inc.* (2008) 159 CA4th 655, 693, 71 CR3d 775, the court held that it was error to refuse to give the following instruction, requested by defendant: "You are not to impose punishment for harms suffered by persons other than the plaintiff before you." Further, a defendant may not be punished for its lawful conduct in other states that does not affect the plaintiff. *BMW of N. Am. v Gore* (1996) 517 US 559, 572, 134 L Ed 2d 809, 824, 116 S Ct 1589. Nevertheless, evidence describing out-of-state transactions may be relevant to determining the degree of reprehensibility of the defendant's conduct. 517 US at 574 n21.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.118B (2) Second Guidepost: Disparity Between Harm Suffered by Plaintiff and Punitives Awarded

§13.118B (2) Second Guidepost: Disparity Between Harm Suffered by Plaintiff and Punitives Awarded

The Supreme Court has declined to establish a bright-line, mathematical formula or ratio of punitive to compensatory damages, explaining that, a punitive damage award generally will be less than ten times the amount of compensatory damages. That ratio may be higher if there is a particularly egregious act that results in a small amount of economic damages. Conversely, if compensatory damages are substantial, a lesser ratio—perhaps only 1:1—could reach the outermost limit of the constitutional guarantee. *State Farm Mut. Auto. Ins. Co. v Campbell* (2003) 538 US 426, 419; 155 L Ed 2d 585, 602; 123 S Ct 1513.

California courts have not rigidly followed the numerical ratio discussed in *State Farm*. For example, in *Simon v San Paolo U.S. Holding Co., Inc.* (2005) 35 C4th 1159, 29 CR3d 379, the California Supreme Court disagreed with the statement in *Diamond Woodworks, Inc. v Argonaut Ins. Co.* (2003) 109 CA4th 1020, 1057, 135 CR2d 736, that, "in the usual case" the U.S. Supreme Court's decisions establish an "outer constitutional limit" of approximately four times the compensatory damages. The *Simon* court stated (35 C4th at 1182):

> We understand the court's statement in *State Farm* that "few awards" significantly exceeding a single-digit ratio will satisfy due process to establish a type of presumption: ratios between the punitive damages award and the plaintiff's actual or potential compensatory damages significantly greater than nine or 10 to one are suspect and, absent special justification (by, for example, extreme reprehensibility or unusually small, hard-to-detect or hard-to-measure compensatory damages), cannot survive appellate scrutiny under the due process clause.

The *Simon* court also held that a punitive damage award of 340 times the compensatory damage award qualified as a "breathtaking" multiplier far outside the "single-digit neighborhood" suggested by *State Farm Mut. Auto. Ins. Co. v Campbell, supra; Simon*, 35 C4th at 1183. The *Simon* court ruled that if an award of punitive damages is constitutionally excessive, the appropriate order is for an absolute reduction, rather than a conditional reduction with the alternative of a new trial. 35 C4th at 1187. In *Simon,* the court reduced the punitive damages to $50,000, just exceeding the largest single-digit ratio amount, which the court stated was "not extraordinary for fraudulent conduct," but not so minor that it could be "completely ignored by the defendant" because even a prosperous company would ordinarily take measures to prevent the recurrence of a $50,000 net loss. 35 C4th at 1189. See also *Walker v Farmers Ins. Exch.* (2007) 153 CA4th 965, 974, 63 CR3d 507 (less reprehensible conduct warrants 1:1 ratio when "handsome" award of emotional distress damages indicated punitive element in compensatory damage award); *Century Sur. Co. v Polisso* (2006) 139 CA4th 922, 966, 43 CR3d 468 (punitive/compensatory ratio of 3.2:1 reflected defendant's reprehensible conduct); *Planned Parenthood, Inc. v American Coalition of Life Activists* (9th Cir 2005) 422 F3d 949, 960 (discussion of punitive/compensatory damage ratios).

In *Exxon Shipping Co. v Baker* (2008) __ US __, 171 L Ed 2d 570, 128 S Ct 2605, the Supreme Court, addressing the award of punitive damages, held that federal maritime law should contain "more rigorous standards than the constitutional limit on punitive damages" (__ US __, 171 L Ed 2d at 594) and concluded that "a 1:1 ratio, which is above the median award, is a fair upper limit" (__ US __, 171 L Ed 2d at 598). The Court emphasized that its inquiry involved "reviewing a jury award for conformity with maritime law, rather than the outer limit allowed by due process." __ US __, 171 L Ed 2d at 591. The Court did not conclude that the Constitution prohibits a punitive damage award greater than the amount awarded for compensatory damages, and cited with approval its prior holdings in *State Farm Mut. Auto. Ins. Co. v Campbell, supra* and *BMW of N. Am. v Gore* (1996) 517 US 559, 134 L Ed 2d 809, 824, 116 S Ct 1589.

Under CC §3295(d), after the defendant's liability for punitive damages is established, evidence of defendant's financial condition, *e.g.,* net worth, may be adduced to the trier of fact to assess the amount of punitive damages. "[T]he defendant's financial condition is an essential factor in setting the amount of a punitive damage award… to serve the goals of retribution and deterrence without exceeding the necessary level of punishment." *Century Sur. Co.,* 139 CA4th at 960.

In *Textron Fin. Corp. v National Union Fire Ins. Co.* (2004) 118 CA4th 1061, 1083, 13 CR3d 586, the appellate court

held that the second *Campbell* "guidepost"—consideration of the disparity between the plaintiff's actual harm and the punitive damage award—must be limited to the amount awarded for the tort claim(s) supporting the punitive damage, and must exclude any sum the plaintiff received for breach of contract.

© The Regents of the University of California

§13.118C (3)Third Guidepost: Court Review of Difference Between Punitives Awarded and Authorized Penalties

The "third guidepost" requires a *court* review of the difference between the punitive damages awarded by the jury and penalties authorized or imposed in comparable cases. The comparison is not a matter for jury consideration. See *Century Sur. Co. v Polisso* (2006) 139 CA4th 922, 959, 43 CR3d 468. In *Century*, the court, found no error in the trial court's use of BAJI 14.72.2, which does not address comparable civil sanctions, nor in the trial court's rejection of a special jury instruction on that issue. Evidence of civil sanctions was properly excluded as irrelevant to the jury's consideration. 139 CA4th at 958. In any event, the appellate court found that the maximum fine imposed by Ins C §790.035 for each willful act of insurer misconduct was not particularly useful information, because the insurer had engaged in a course of conduct involving many prohibited acts over a 5-year period. 139 CA4th at 967.

© The Regents of the University of California

§13.118D (4) Aggregate Disgorgement of Profits Theory Prohibited

An award of punitive damages may not be based on an aggregate disgorgement of profits theory. *Johnson v Ford Motor Co.* (2005) 35 C4th 1191, 29 CR3d 401. Although repeated acts of similar misconduct and the profitability of that conduct is relevant to the issue of reprehensibility and though disgorgement of profits earned from the wrongful act committed against the plaintiff is permissible, calculating punitive damages in an individual tort case based on the profits from similar torts against other individuals "creates possibilities for unfairness—to the defendant and other possible claimants both—which may be of constitutional dimension." 35 C4th at 1208.

© The Regents of the University of California

§13.118E (5) Evidence of Defendant's Net Worth Required

To serve the goals of punishment and deterrence, a punitive damage award must be large enough to deter future bad conduct, without exceeding the amount necessary for punishment. *Century Sur. Co. v Polisso* (2006) 139 CA4th 922, 967, 43 CR3d 468; *Simon v San Paolo U.S. Holding Co., Inc.* (2005) 35 C4th 1159, 1185, 29 CR3d 379. In *Century Sur. Co.*, the court held that evidence of the defendant's net worth was an essential factor in the punitive damage phase of the trial. 139 CA4th at 960. See *Adams v Murakami* (1991) 54 C3d 105, 110, 284 CR 318; see also CC §3295(d). Specifically, the court found that a punitive damage award of 3.2 percent of the defendant's net worth was appropriate, because a smaller award "would not amount to much more than a slap on the wrist." 139 CA4th at 967. See also *Bardis v Oates* (2004) 119 CA4th 1, 26, 14 CR3d 89 (punitive damage award of less than 1 percent of defendant's net worth "tantamount to a slap on the wrist").

© The Regents of the University of California

§13.119 C. Duty of Good Faith Is Mutual; No Cause of Action for "Reverse Bad Faith"

The duty of good faith between insurer and insured is mutual. Counsel for the insured, as the insured's agent, is bound by the duty of good faith in all matters concerning resolution of the underlying claim. Although the insured may not be held liable for damages for "reverse bad faith" (*Kransco v American Empire Surplus Lines Ins. Co*. (2000) 23 C4th 390, 402, 97 CR2d 151), the insured's "bad faith" may be asserted as a defense to contract claims against the insurer. *Agricultural Ins. Co. v Superior Court* (1999) 70 CA4th 385, 82 CR2d 594. In addition, the insurer may file suit or cross-complain against the insured for fraud and may seek damages, including punitive damages. 70 CA4th at 404.

PRACTICE TIP: Whether counsel represents the claimant or the insurer, the attorney's letters, conversations, and other interactions, even after a suit has been filed, may become evidence in litigation over the duty of good faith. *White v Western Title Ins. Co.* (1985) 40 C3d 870, 885, 221 CR 509. As a potential witness, counsel should take care not to say or write anything that he or she would not wish to see enlarged as a trial exhibit.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.120 D. Genuine Dispute Doctrine

§13.120 D. Genuine Dispute Doctrine

The "genuine dispute" doctrine, also called the "genuine issue" doctrine, is a rapidly evolving area of bad faith law. Bad faith liability may not be imposed if there is a genuine dispute over the insurer's liability under the policy. If an insurer denies or delays payment of policy benefits because it has a genuine dispute with its insured about the existence of coverage or the amount of the insured's claim, the insurer is not liable for bad faith, even though it may be liable for breach of contract. *McCoy v Progressive W. Ins. Co.* (2009) 171 CA4th 785, 793, 90 CR3d 74; *Chateau Chamberay Homeowners Ass'n v Associated Int'l Ins. Co*. (2001) 90 CA4th 335, 347, 108 CR2d 776; *R&R Sails, Inc. v Insurance Co. of the State of Pennsylvania* (SD Cal 2009) 610 F Supp 2d 1222, 1230. The doctrine may be applied whether the genuine dispute is based on legal or factual issues. *Fraley v Allstate Ins. Co.* 81 CA4th 1282, 1292, 97 CR2d 386; *Chateau Chamberay Homeowners Ass'n,* 90 CA4th at 348. However, if the dispute is based on a conflict of expert opinions, the doctrine does not apply if any of the following are true (90 CA4th at 348):

- The insurer misrepresented the nature of the investigation;
- The insurer's employees lied during depositions or to the insured;
- The insurer dishonestly selected its experts;
- The insurer's experts were unreasonable; or
- The insurer failed to conduct a thorough investigation.

In *McCoy v Progressive West Ins. Co.* (2009) 171 CA4th 785, 792, 90 CR3d 74 the insurer proposed jury instructions which were based on the foregoing factors and which stated that a genuine dispute does not constitute bad faith. The appellate court affirmed the trial court's refusal to give the instructions, because the genuine dispute doctrine is subsumed within the concept of what is reasonable and unreasonable, as set forth in CACI 2331 and 2332. Therefore, no further instruction was necessary.

NOTE: Counsel could argue that the applicable elements of the "genuine issue doctrine" deserve a special instruction to the jury, just like the "advice of counsel" defense. Case law recognizes that the "advice of counsel defense" is not a true affirmative defense, but rather negates an essential element of the insured's cause of action for bad faith. *State Farm Mut. Auto. Ins. Co. v Superior Court* (1991) 228 CA3d 721, 725, 279 CR 116. Nevertheless, there is a specific CACI instruction, 2335, on that issue.

A mistaken withholding of policy benefits, such as an inadvertent failure to indemnify, may qualify under the genuine dispute doctrine, but the doctrine does not encompass the insurer's duty to defend, which is a much broader duty. *Century Sur. Co. v Polisso* (2006) 139 CA4th 922, 950, 43 CR3d 468.

© The Regents of the University of California

§13.121 E. No Cause of Action for Breach of Fiduciary Duty

Insureds cannot base claims on an alleged breach of fiduciary duty. See, *e.g., Vu v Prudential Prop. & Cas. Ins. Co.* (2001) 26 C4th 1142, 1150, 113 CR2d 70 ("[B]ut while these 'special' duties [characteristic of an insurer-insured relationship] are akin to, and often resemble, duties which are also owed by fiduciaries, the fiduciary-like duties arise because of the unique nature of the insurance contract, not because the insurer is a fiduciary."); *Tran v Farmers Group, Inc.* (2002) 104 CA4th 1202, 1212, 128 CR2d 728 ("[A]n insurer's breach of its 'fiduciary-like duties' is adequately redressed by a claim for breach of the covenant of good faith and fair dealing implied in the insurance contract"); *Love v Fire Ins. Exch*. (1990) 221 CA3d 1136, 1147, 271 CR 246; *Henry v Associated Indem. Corp.* (1990) 217 CA3d 1405, 1418, 266 CR 578.

© The Regents of the University of California

§13.122 F. Unfair Competition Claims Under Bus & P C §17200

The Unfair Competition Law (UCL) (Bus & P C §§17200-17210), provides equitable relief for unlawful, unfair, or fraudulent business practices. Remedies include injunctive relief, civil penalties, and restitution of property or money obtained as a result of the alleged unfair business practice. Bus & P C §§17203, 17206. However, compensatory damages or attorney fees are not available to private litigants under the UCL. See *Korea Supply Co. v Lockheed Martin Corp.* (2003) 29 C4th 1134, 1144, 131 CR2d 29; *Cortez v Purolator Air Filtration Prods., Co.* (2000) 23 C4th 163, 173, 96 CR2d 518; *Cel-Tech Communications, Inc. v Los Angeles Cellular Tel. Co.* (1999) 20 C4th 163, 179, 83 CR2d 548. Moreover, a court cannot order disgorgement into a fluid recovery fund (*i.e.,* any residue remaining after payment of individual claims) under Bus & P C §17200. See *Kraus v Trinity Mgmt. Servs., Inc*. (2000) 23 C4th 116, 137, 96 CR2d 485 (fluid recovery fund, consisting of defendants' illegal profits, "organized and administered for the purpose of providing financial assistance for the advancement of legal rights and interests of residential tenants in the City and County of San Francisco," held to be unavailable under UCL).

Insureds suing for bad faith often include a §17200 cause of action because the UCL will not support a private right of action against an insurer based solely on a violation of the Unfair Insurance Practices Act (Ins C §790.03(h)). *Manufacturers Life Ins. Co. v Superior Court* (*Weil Ins. Agency*) (1995) 10 C4th 257, 283, 41 CR2d 220; *R&R Sails, Inc. v Insurance Co. of the State of Pennsylvania* (SD Cal 2009) 610 F Supp 2d 1222, 1233. See also California Title Insurance Practice §§11.29-11.54 (2d ed Cal CEB 1997). In *State Farm Fire & Cas. Co. v Superior Court* (1996) 45 CA4th 1093, 53 CR2d 229, however, the Second District Court of Appeal held that while an insured may not base a §17200 claim on violations of Ins C §790.03, an insured may base a §17200 claim on allegations of common law fraud and bad faith. 45 CA4th at 1108. However, in *Textron Fin. Corp. v National Union Fire Ins. Co.* (2004) 118 CA4th 1061, 1070, 13 CR3d 586, the Fourth District Court of Appeal held that the insurer's alleged use of misleading documents and misrepresentation of both the terms of the insurance policies and the insurer's obligations under them "are the type of activities covered by the [Unfair Insurance Practices Act (Ins C §790.03(h))]," and could not form the basis for a §17200 claim.

In *Hangarter v Provident Life & Acc. Ins. Co.* (9th Cir 2004) 373 F3d 998, the Ninth Circuit held an insured who no longer had a contractual relationship with the insurer and could not demonstrate a "real or immediate threat of an irreparable injury" did not have standing under U.S. Const art III to pursue an action for injunctive relief under §17200, even if the insured would have been able to pursue the claim in state court. 373 F3d at 1021. See also California Liability Insurance Practice: Claims & Litigation §28.29 (Cal CEB 1991).

NOTE: In *Cel-Tech Communications, Inc. v Los Angeles Cellular Tel. Co.* (1999) 20 C4th 163, 179, 83 CR2d 548, the supreme court disapproved as overbroad the definition of "unfair" used in *State Farm Fire & Cas. Co. v Superior Court, supra,* but the court did not disapprove of its holding that common law fraud and bad faith can support a §17200 claim. Nevertheless, the *State Farm* case and the *Textron* case do not appear to be reconcilable. It appears the supreme court will ultimately have to decide this issue.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.123 G. Other Statutory Violations

§13.123 G. Other Statutory Violations

Insureds no longer have standing to assert a violation of the Unfair Insurance Practices Act (Ins C §790.03(h)). See *Moradi-Shalal v Fireman's Fund Ins. Co.* (1988) 46 C3d 287, 250 CR 116 (insured cannot base private cause of action solely on violation of §790.03); see also *Manufacturers Life Ins. Co. v Superior Court (Weil Ins. Agency*) (1995) 10 C4th 257, 41 CR2d 220 (insureds cannot use Bus & P C §17200 to plead cause of action based on violation of §790.03(h), because to do so would undermine *Moradi-Shalal*).

NOTE: Although Ins C §1861.03(a) has made insurers subject to all of California's antitrust, unfair competition, and unfair business practices statutes, it does not itself create a private remedy for damages. *Maler v Superior Court* (1990) 220 CA3d 1592, 1597, 270 CR 222.

In *Fairbanks v Superior Court* (2009) 46 C4th 56, 61, 92 CR3d 279, the supreme court held that the Consumer Legal Remedies Act (CLRA) (CC §§1750-1784), which does allow a private right of action for unfair or deceptive practices, does not apply to life insurance because it is not a "good" or a "service" within the meaning of the Act. See also *Broberg v The Guardian Life Ins. Co. of Am.* (2009) 171 CA4th 912, 925, 90 CR3d 225 (life insurance is not a "good" or a "service" within the meaning of the CLRA).

NOTE: In contrast to life insurance, liability insurance typically includes a contractual promise to "defend" the insured against specified claims. The supreme court has characterized such a duty to defend as a promise to render a service, distinguishable from the promise to indemnify after defense costs have been incurred. *Crawford v Weather Shield Mfg., Inc.* (2008) 44 C4th 541, 553, 79 CR3d 721. Whether *Fairbanks* and *Broberg* will be limited to life insurance or extended to other types of insurance remains to be seen.

© The Regents of the University of California

XI. EMERGING ISSUES REGARDING PROPERTY INSURANCE

§13.124 A. Terrorism

The Terrorism Risk Insurance Act of 2002 (TRIA) (Pub L 107-297, §101(b), 116 Stat 2322) created a temporary federal program to establish a "transparent system of shared public and private compensation for insured losses resulting from acts of terrorism." TRIA has twice been extended, most recently on December 26, 2007. See the Terrorism Risk Insurance Program Reauthorization Act of 2007 (Pub L 110-160, 121 Stat 1839). Under the extension, the Treasury Department requires that all insurers participate in the federal program through December 31, 2014. See §§13.125-13.129 for discussion of the risk insurance program.

The ISO and the American Association of Insurance Services (AAIS), an insurance industry technical support organization, have filed four types of endorsements to bring policies into compliance with the Act. The Act exempts such endorsements from any state's requirement that its insurance department has the right to approve the policy forms. TRIA §106(a)(2)(B).

The ISO has also filed a fifth type of endorsement that excludes certified acts of terrorism losses, with an exception for certain fire losses. In addition, the AAIS has filed endorsements to exclude noncertified acts of terrorism losses. For information about the AAIS, see the AAIS website listed in the Directory.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.125 1. All Commercial Insurers Must Participate [Deleted]

§13.125 1. All Commercial Insurers Must Participate [Deleted]

Terrorism material has been summarized and consolidated in §13.124.

© The Regents of the University of California

§13.126 2. Commercial Insurers' Terrorism Exclusions Are Void [Deleted]

Terrorism material has been summarized and consolidated in §13.124.

© The Regents of the University of California

§13.127 3. Characteristics of "Acts of Terrorism" [Deleted]

Terrorism material has been summarized and consolidated in §13.124.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.128 4. Certification by the Secretary of the Treasury [Deleted]

§13.128 4. Certification by the Secretary of the Treasury [Deleted]

Terrorism material has been summarized and consolidated in §13.124.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.129 5. Types of New ISO Terrorism Exclusions [Deleted]

§13.129 5. Types of New ISO Terrorism Exclusions [Deleted]

Terrorism material has been summarized and consolidated in §13.124.

© The Regents of the University of California

§13.130 B. Mold

Litigation involving mold claims has become commonplace. Although mold existed long before mankind, many experts blame current building techniques—*e.g.,* airtight construction of commercial buildings and residences to conserve energy and increase comfort—for increasing indoor moisture levels and creating other conditions that facilitate the growth of mold. Although scientists apparently still disagree about causation, toxic molds have been blamed for a variety of physical ailments, ranging from flu-like symptoms to death.

NOTE: California adopted the Toxic Mold Protection Act of 2001 (Health & S C §§26100-26157), which imposes certain disclosure and remediation requirements on owners and transferors regarding the presence of mold in their buildings. See §4.82.

The insurance industry considers mold caused by excessive humidity, condensation, or flooding to be a maintenance issue. For that reason, mold is not covered under standard homeowners' or commercial property policies unless the mold is the result of a covered peril. Mold may be a distinct peril under an insurance policy, if it is not caused by a sudden discharge of water. See *DeBruyn v Superior Court* (2008) 158 CA4th 1213, 1223, 70 CR3d 652.

NOTE: In some policies, mold may be a covered cause of loss. In *Freedman v State Farm Ins. Co.* (2009) 173 CA4th 957, 964, 93 CR3d 296, an endorsement to the policy provided limited coverage for losses caused by "fungus," which was defined to included "any type of fungi, including mold or mildew." However, the court held there was no coverage for the mold damage, because the mold was caused by exclusions for contractor negligence, corrosion, or seepage or leakage of water from a plumbing system. 173 CA4th at 965.

A 2004 report by the California Department of Insurance found that 70 percent of multi-peril homeowners' insurers use mold exclusions or special limits for losses due to mold. Even the National Flood Insurance Program's Dwelling Policy (under the National Flood Insurance Act (42 USC §§4001-4129); see §13.53) excludes coverage for "water, moisture, mildew, or mold damage caused by the policyholder's failure to inspect and maintain the insured property after the flood waters recede." Dwelling Policy ¶12, §5, Exclusion D.4.b.(3). (The Dwelling Policy can be viewed at the FEMA website, which can be found in the Directory.)

For a comprehensive treatment of issues concerning mold litigation, see Handling Mold Litigation in California (Cal CEB Action Guide September 2007).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.131 1. As a Covered Cause of Loss [Deleted]

§13.131 1. As a Covered Cause of Loss [Deleted]

Mold material has been summarized and consolidated in §13.130.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.132 2. Potentially Applicable Exclusions [Deleted]

§13.132 2. Potentially Applicable Exclusions [Deleted]

Mold material has been summarized and consolidated in §13.130.

© The Regents of the University of California

§13.133 C. Sick-Building Syndrome

Increasingly, people claim they are being made sick by the buildings in which they live or work. Many products, including carpet fibers, flooring adhesives, wall coverings, or air circulation systems, either alone or in combination, are being blamed. Unfortunately, most of the insurance issues related to "sick-building syndrome" claims are still unresolved.

The first coverage issue regarding sick-building syndrome claims under a property policy will be whether there is a covered cause of loss. A named-perils policy will likely not list a peril that applies to sick-building claims. The author is not aware of any reported California case that has decided whether a "sick building" loss is a "direct physical loss."

In "sick-building" claims, there will undoubtedly not only be a dispute over when the loss was "manifest," but also which trigger should be applied, and whether the loss was known and thus not covered by the policy. The author is not aware of any reported California case that has addressed these issues. On direct physical loss and triggers applied to losses, see §§13.73-13.83; on the manifestation rule, see §13.80.

Several exclusions may bar coverage for "sick-building" claims. For example, the pollution exclusion (Exclusion 2.l in the ISO Causes of Loss—Special Form (CP 10 30 04 02)) may apply if the injury-causing product is found to be an "irritant," a "contaminant," or a "chemical" within the definition of "pollutants." The exclusions for "fungus, decay, deterioration, hidden or latent defect or any quality in property that causes it to damage or destroy itself" (Exclusion 2.d in the ISO Causes of Loss—Special Form (CP 10 30 04 02)) may apply to certain claims. The author is not aware of any reported California cases on these issues.

© The Regents of the University of California

§13.134 1. Direct Physical Loss [Deleted]

Sick Building Syndrome material has been summarized and consolidated in §13.133.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.135 2. Manifested During the Policy Term [Deleted]

§13.135 2. Manifested During the Policy Term [Deleted]

Sick Building Syndrome material has been summarized and consolidated in §13.133.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/13 Property Insurance/§13.136 3. Potentially Applicable Exclusions [Deleted]

§13.136 3. Potentially Applicable Exclusions [Deleted]

Sick Building Syndrome material has been summarized and consolidated in §13.133.

© The Regents of the University of California

§13.137 D. Chinese Drywall

Numerous unresolved insurance issues are raised by complaints of property damage and illness allegedly caused by chemical compounds emitted from drywall imported from China. According to a press release issued in support of S 739, the Drywall Safety Act of 2009, more than 550 million pounds of drywall have been imported to the U.S. from China since 2006. The Consumer Product Safety Commission (CPSC) has determined that over 5.5 million sheets of drywall were imported to the U.S. from China during 2006 alone. More than 800 complaints from at least 23 states have been filed with the CPSC regarding Chinese drywall. See Directory for the internet address of CPSC's website for information regarding Chinese drywall.

According to the CPSC, in addition to human symptoms, complaints regarding property damage related to Chinese drywall include obnoxious odors emanating from the drywall; intermittent operation or premature failure of electric and electronic appliances and devices; corrosion of electrical components; and corrosion and premature failure of gas service and fire safety components.

Unfortunately, almost all the insurance issues related to Chinese drywall claims are unresolved.

© The Regents of the University of California

§13.138 1. Direct Physical Loss

The first coverage issue regarding Chinese drywall claims under a property policy will be whether there is a covered cause of loss. A named-perils policy will likely not list a peril that applies to Chinese drywall. For example, neither the ISO Causes of Loss—Basic Form (CP 10 10 04 02) nor the ISO Causes of Loss—Broad Form (CP 10 20 04 02) lists any "covered cause of loss" that would extend to such a claim. An all-risk policy, such as the ISO Causes of Loss—Special Form (CP 10 30 04 02) or the ISO Homeowners 3 - Special Form (HO 00 03 10 00), extends coverage to all nonexcluded perils but requires that the loss be a "direct physical loss."

A key issue, then, is whether there has been a "direct physical loss" See §13.73. Despite existing case law (*e.g., State Farm Fire & Cas. Co. v Superior Court* (1989) 215 CA3d 1435, 1445, 264 CR 269 (poor workmanship merely diminishes the value of property and is not "direct physical loss")), creative arguments based on simple facts could be tried. The Chinese drywall contaminates the home with odors and noxious chemicals (see §13.139); causes "direct physical damage" to metal components and all types of electrical and electronic components; and creates an intolerable safety risk and renders the property uninhabitable (see §13.140).

© The Regents of the University of California

§13.139 a. Odor; Release of Harmful Compounds

Although there have been no reported cases involving insurance coverage for odors caused by Chinese drywall, cases from other jurisdictions have held that foul odors that permeate the property may constitute physical damage. See *Farmers Ins. Co. v Trutanich* (Or App 1993) 123 Or App 6, 858 P2d 1332, 1335 (odors caused by meth lab); *Essex Ins. Co. v BloomSouth Flooring Corp*. (1st Cir 2009) 562 F3d 399 (applying Massachusetts law, to defective carpet under CGL policy).

An insured might also argue that Chinese drywall releases harmful compounds into the home, much in the same way that asbestos fibers may be released. Several cases have held that an asbestos release constitutes "direct physical loss." See, *e.g*., *Sentinel Management Co. v New Hampshire Ins. Co.* (Minn App 1997) 563 NW2d 296, 300; *Yale Univ. v CIGNA Ins. Co*. (D Conn 2002) 224 F Supp 2d 402, 4121; *BellSouth Telecommunications, Inc. v W.R. Grace & Co*. (2d Cir 1996) 77 F3d 603; *Port Auth. of New York & New Jersey v Affiliated FM Ins. Co.* (3rd Cir 2002) 311 F3d 226, 235-236.

© The Regents of the University of California

§13.140 b. Safety and Habitability

Significantly some California cases have held there is coverage for potential damage rendering a dwelling uninhabitable. See *Strickland v Federal Ins. Co.* (1988) 200 CA3d 792, 800, 246 CR 345 (risk of damage from landslide with policy that extended coverage to all risk of physical loss) and cases cited in *Strickland*. However, these cases involved policies that extended coverage to all risk of physical loss; none of them discussed any provision regarding "direct physical loss."

An insured might argue that Chinese drywall poses a risk to electrical components, including deterioration of connections. A degraded connection could develop hot spots resulting in overheating and possibly fire. Other concerns involve erosion of copper conductors over time. If the corrosion progressively eats away at a wire, the wire would eventually lose its capacity to carry current and start to overheat or become physically weak and break. In addition, contamination from Chinese drywall may cause damage to electronic components on printed circuit boards causing failure of protective devices like ground fault circuit interrupters, arc-fault circuit interrupters, and smoke alarms, which can present shock and fire hazards from the loss of protection provided by these devices. Contamination from Chinese drywall may also cause corrosion of gas service components, causing a potential gas leak due to corrosive pitting of piping could present a fire or explosion hazard. For further discussion of "direct physical loss," see §13.73.

© The Regents of the University of California

§13.141 2. Possible Applicable Exclusions

Insurers will likely raise a number of exclusions to claims involving Chinese drywall. These may include:

- **Pollutants.** Many policies exclude pollutants. But see *McKinnon v Truck Ins. Exch.* (2003) 31 C4th 635, 653, 3 CR3d 228 (term "pollutant" in absolute pollution exclusion in CGL policy limited to "conventional environmental pollution," and did not encompass "ordinary acts of negligence involving harmful substances"). No reported case has decided whether the chemical compounds released by Chinese drywall are pollutants. For further discussion of the pollution exclusion, see §13.86.
- **Wear and Tear, Decay, Latent Defects.** Homeowners and business owners policies typically contain exclusions for damage caused by "wear and tear," "deterioration," and "latent defect [or] inherent vice." See, *e.g., Scott v Continental Ins. Co.* (1996) 44 CA4th 24, 35, 51 CR2d 566 (faults, flaws, and irregularities in design, faulty construction, or weakness of materials); *Chadwick v Fire Ins. Exch*. (1993) 17 CA4th 1112, 1126, 21 CR2d 871 (substandard design and construction of house's wall and floor framing); *Murray v State Farm Fire & Cas. Co*. (1990) 219 CA3d 58, 268 CR 33 (deterioration of copper water pipe caused by electrolysis over 17-year period, though expected to last 50 years, excluded as wear and tear); *Brodkin v State Farm Fire & Cas. Co.* (1989) 217 CA3d 210, 217, 265 CR 710 (slow disintegration of concrete foundation from corrosive soil conditions).
- **Faulty Design, Workmanship, Materials.** There are exclusions for loss caused by faulty, inadequate or defective design, specifications, workmanship, repair, construction, renovation, remodeling, or materials used in repair, construction, renovation or remodeling, or maintenance of all or part of any property. See, *e.g., Freedman v State Farm Ins. Co.* (2009) 173 CA4th 957, 93 CR3d 296 (precluded damage caused by contractor leading to corrosion, leakage, and mold); *Davis v United Servs. Auto. Ass'n* (1990) 223 CA3d 1322, 273 CR 224 (contractor negligence); *Sapiro v Encompass Ins.* (ND Cal 2004) 221 FRD 513, 521 (exclusion precluded coverage for damage caused by moisture, water damage, and fungi resulting from gap between flashing and stucco of home).

© The Regents of the University of California

14

Liability Insurance: Selected Issues Pertinent to Sales

Timothy R. Sullivan

I. INTRODUCTION
- A. Chapter Scope; Selecting Insurance Products §14.1
- B. ISO Forms Versus Manuscript Policies §14.2
- C. Types of Liability Insurance Pertinent to Real Property Sales
  - 1. Commercial General Liability §14.3
  - 2. Businessowners Liability §14.4
  - 3. Owners and Contractors Protective §14.5
  - 4. Architects and Engineers Professional Liability §14.6
  - 5. Contractors Professional Liability §14.7
  - 6. Real Estate Agent's Errors and Omissions §14.8
  - 7. Representations and Warranties Insurance §14.9
  - 8. Homeowners §14.10
- D. Issues Arising Under Various Policies §14.11

II. SPECIAL ISSUES: OCCURRENCE; CLAIMS MADE; AND CLAIMS MADE AND REPORTED POLICIES
- A. Occurrence Policies §14.12
- B. "Claims Made" Policies §14.13
- C. "Claims Made and Reported" Policies §14.14
- D. What Is a "Claim"? §14.14A
- E. Extended Reporting Period §14.15
- F. Retroactive Date §14.16

III. SPECIAL ISSUES: COMMERCIAL GENERAL LIABILITY §14.17
- A. "Occurrence" or "Accident" §14.18
  - 1. "Accidental" and "Negligent" Not Synonymous §14.19
    - a. Examples of "Accidental" Conduct §14.20
    - b. Examples of Non-"Accidental" Conduct §14.21
  - 2. Failure to Disclose; Misrepresentations Upon Sale §14.22
  - 3. Latent Defects §14.23
  - 4. Negligent Construction; Negligent Design §14.24
- B. Property Damage; Defective or Faulty Materials §14.25
  - 1. Damages §14.25A
  - 2. Physical Injury to Other Property §14.26
  - 3. No Physical Injury to Other Property §14.27
- C. Bodily Injury §14.28
  - 1. Emotional Distress Without Physical Injury §14.29
  - 2. Emotional Distress With Physical Injury §14.30
- D. Insured Parties §14.31
  - 1. Named Insured; Additional Insured Distinguished §14.32
    - a. Fictitious Names §14.33
    - b. Partnerships §14.34
    - c. "The Insured," "An Insured," or "Any Insured" §14.35
  - 2. Additional Named Insureds §14.36
  - 3. Additional Insured §14.37
    - a. Sole Negligence §14.38
    - b. Does Duty to Defend Extend to Entire Action? §14.39
    - c. Statutory Limit on Indemnity Provisions §14.40
    - d. Certificate of Insurance §14.41
    - e. ISO Additional Insured Endorsements; Exclusions §14.42
      - (1) "Arising Out of" Versus "Caused, in Whole or in Part, by" §14.43
      - (2) "Ongoing Operations" §14.44
      - (3) "Acts or Omissions" §14.45

f. Manuscript Additional Insured Endorsements §14.46
E. Effect of Stated Policy Period on Coverage §14.47
1. Continuous or Progressive Loss §14.48
2. Examples of Continuous and Progressive Damage §14.49
3. "Known Injury or Damage" Provisions in Post-1998 ISO CGL Policies §14.49A
a. ISO Policy Changes After *Montrose II* §14.49B
b. Other Anti-*Montrose II* Provisions §14.49C
4. Number of Occurrences §14.49D
5. After-Acquired Property §14.50
F. Liability Assumed by the Insured §14.51
G. Duty to Defend §14.52
1. Broader Than Duty to Indemnify §14.53
2. Extends to Entire Claim §14.54
3. Extrinsic Evidence May Support Duty to Defend §14.55
4. Reimbursement of Defense Costs §14.56
H. Products or Completed Operations Hazard §14.57
I. Property Damage Exclusions §14.58
1. Property the Insured Owns, Rents, or Occupies §14.59
2. Alienated Premises §14.60
3. Property Loaned to Insured §14.61
4. Property Damage to Personal Property in Care, Custody, or Control of the Insured §14.62
5. Work Performed §14.63
6. Faulty Workmanship
a. No Coverage for Defective Building Parts Caused by Work Incorrectly Performed §14.64
b. Damage to Building Caused by Removal of Defective Materials and Faulty Workmanship Distinguished §14.65
7. Product Exclusion: Damage to Your Product §14.66
8. Work Completed Exclusion: Damage to Your Work §14.67
9. Damage to "Impaired Property" §14.68
J. The Pollution Exclusion §14.68A
K. Personal and Advertising Injury
1. Insuring Language §14.69
2. Exclusions §14.70

IV. SPECIAL ISSUES: BUSINESSOWNERS LIABILITY §14.71

V. SPECIAL ISSUES: REAL ESTATE AGENTS' ERRORS AND OMISSIONS LIABILITY POLICY §14.72
A. Claims Made §14.73
B. Representative Insuring Clause §14.74
C. Exclusions §14.75

VI. SPECIAL ISSUES: REPRESENTATIONS AND WARRANTIES INSURANCE §14.76
A. Representative Insuring Language §14.77
B. Claims Made §14.78
C. Exclusions §14.79

VII. SPECIAL ISSUES: HOMEOWNERS LIABILITY
A. Insuring Language §14.80
B. Exclusions §14.81
1. Business §14.82
2. Professional Services §14.83
3. Noninsured Location §14.84
4. Arising Out of the Sale §14.85

© The Regents of the University of California

I. INTRODUCTION

§14.1 A. Chapter Scope; Selecting Insurance Products

This chapter provides an overview of the common types of liability insurance related to real property transfers and common insurance issues that may arise from these transfers. It is beyond the scope of this chapter to discuss in detail all the available policies or all the insurance issues that may arise.

In drafting transactional documents, attorneys often add requirements that a particular party be indemnified by the other party and included as an additional named insured on the other party's insurance policy. As part of this process, the attorney may review available insurance products offered by an agent or broker to formulate a list of potential risks for which coverage might be needed. More attorneys are participating in the risk-analysis phase of transactions and assisting clients in a general way with insurance selection. Much of this chapter is dedicated to the history of policy drafting and coverage analysis derived from case law, because it is essential for attorneys engaged in risk management to understand the evolution of policy language and interpretations given to insurance policies by the courts.

WARNING: Even when a lawyer has enough knowledge of available types of insurance to recognize those transactions and issues in which insurance may play a role, the lawyer should delegate primary responsibility for the ultimate selection and purchase of insurance to an experienced insurance agent or broker.

For a detailed discussion of liability insurance enforcement, including claims process, duty to defend, and related litigation, see California Liability Insurance Practice: Claims & Litigation (Cal CEB 1991).

© The Regents of the University of California

§14.2 B. ISO Forms Versus Manuscript Policies

The Insurance Services Office (ISO) is a nonprofit trade association that provides rating, statistical, and actuarial policy forms and related drafting services to approximately 3000 nationwide property or casualty insurers. As discussed in chap 13 in reference to property insurance, the ISO publishes standard forms of liability policies that are used by many insurers. Policy forms developed by the ISO are approved by its constituent insurance carriers and then submitted to state agencies for review. Most carriers use the basic ISO forms, at least as the starting point for their general liability policies. *Montrose Chem. Corp. v Admiral Ins. Co.* (1995) 10 C4th 645, 671 n13, 42 CR2d 324. For information about the ISO, see the ISO website listed in the Directory.

There are too many different types of liability policies to discuss them all in this chapter. This chapter refers to ISO forms for typical language and form designations and numbers. The letters at the beginning of the ISO designation refer to the respective policy type: "CG" for Commercial General Liability, "BP" for Businessowners Coverage Form (liability), "HO" for Homeowners, and so on. The last two sets of digits indicate the month and year the form was first released for use, *i.e.,* "12 04" refers to December 2004. Thus, CG 00 01 12 04 is the December 2004 version of the Commercial General Liability policy; note that some of the references in the following sections may be in truncated form, *e.g.,* CG 00 01. This is a convenient way to determine whether the policy contains the most recent policy forms. A typical policy will contain one or more basic forms, plus additional forms for declarations, conditions, optional coverages, and exclusions.

NOTE: Throughout this chapter, many types of policies and endorsements are described. The quoted material in this chapter (pertaining to covered claims, occurrences, exclusions, or definitions) is common to or typical of most policies of that type being discussed, whether it is an ISO policy or another version.

Often insurers draft their own forms, using parts of the ISO policy language and revising other parts. Insurers' policy forms use different designations and numbers.

PRACTICE TIP: Practitioners should not assume that all forms are the same, or even similar. In each transaction, the insurance policy should be reviewed carefully to determine which risks are covered and which are not. Although this lack of uniformity makes it difficult to draft contract provisions specifically, because not all insurers will use the same policy form designation and number, the difference in policies means some policies may offer broader coverage. Moreover, caution should be used in referring to specific policy forms in real estate contracts, because that may limit the insurer's ability to provide the most appropriate coverage. In addition, reference to specific policy forms may create problems if a form is changed or a specific edition is no longer available.

© The Regents of the University of California

C. Types of Liability Insurance Pertinent to Real Property Sales

§14.3 1. Commercial General Liability

The ISO Commercial General Liability Form (CG 00 01) is a very widely used form. Liability Coverage is divided into two sections. Coverage A affords coverage for "bodily injury" (see §14.28) and "property damage" (see §14.25) caused by an "occurrence" (see §14.18). Coverage B provides coverage for "advertising injury" and "personal injury" (see §§14.69-14.70).

The CG 00 01 version is an "occurrence-based" form, but CG 00 02 is a "claims made" form. See §§14.12-14.13.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.4 2. Businessowners Liability

§14.4 2. Businessowners Liability

The ISO Businessowners Coverage Form (BP 00 03 07 02) is another commonly used form. Unlike the CGL policy, the Businessowners policy (referred to in the industry as BOP) provides both property coverage and liability coverage. However, like the CGL form, the Businessowners form provides liability coverage for "bodily injury" (see §14.28) and "property damage" (see §14.25) caused by an "occurrence" (see §14.18), as well as for "advertising injury" and "personal injury" (see §§14.69-14.70). The insuring language, exclusions, and definitions of the Businessowners policy are, for the most part, identical to the comparable provisions of the CGL policy. For that reason, the issues that arise under the Businessowners policy in connection with a real estate transaction will be substantially similar to those under a CGL policy.

© The Regents of the University of California

§14.5 3. Owners and Contractors Protective

The ISO Owners and Contractors Protective (OCP) policy (CG 00 09 12 04) is a stand-alone policy that may be obtained in conjunction with a CGL policy; it is usually purchased to comply with contract provisions that require one party to indemnify and purchase insurance coverage for another. A general contractor may purchase OCP coverage that names the owner or developer as the named insured, or a subcontractor may purchase OCP coverage that names the general contractor as the named insured. In either case, the party purchasing the policy obtains no coverage under the OCP policy. The alternative would be for the subcontractor to make the general contractor an additional insured on the subcontractor's policy, or for the general contractor to make the owner an additional insured on the general contractor's policy. The definitions of "bodily injury" (see §14.28), "property damage" (see §14.25), and "occurrence" (see §14.18) are the same as those found in the 2004 ISO CGL policy.

© The Regents of the University of California

§14.6 4. Architects and Engineers Professional Liability

To obtain coverage for professional liability, architects and engineers typically buy a separate malpractice insurance policy in conjunction with a CGL policy. Often, this is called an Architects and Engineers Professional Liability (AEPL) policy. There is no standard-language form for such a policy. Unlike CGL or BOP policies, AEPL policies typically do not limit coverage to "bodily injury," "property damage," or "personal and advertising injury." They typically insure against claims arising from "professional services." See, *e.g.,* ISO CG 22 43. They are written on a "claims made" basis (see §14.13; see also "extended reporting period," discussed in §14.15).

© The Regents of the University of California

§14.7 5. Contractors Professional Liability

There is no standard-language ISO form for a Contractors Professional Liability policy. However, most have common features. Most (if not all) impose a duty to defend on the insurer (see §§14.52-14.56). Most (if not all) are written on a "claims made" basis (see §14.13). They are frequently obtained in conjunction with CGL and other policies. Unlike CGL or BOP policies, a Contractors Professional Liability policy typically does not limit coverage to "bodily injury," "property damage," or "personal and advertising injury." Coverage is provided for "wrongful acts," typically defined as a negligent act, error, or omission in the performance of professional services for others, such as construction management. Most Contractors Professional Liability policies condition the insurer's right to settlement on the insured's consent, but impose a penalty if the insured withholds consent.

© The Regents of the University of California

§14.8 6. Real Estate Agent's Errors and Omissions

Like other errors and omissions policies, coverage for real estate agents and brokers is almost always written on a "claims made" basis. See §14.13; see also "extended reporting period," discussed in §14.15. Liability coverage extends to claims arising out of any act, error, omission, or "personal injury" in the rendering of or failure to render "professional services." It is a stand-alone policy and is usually obtained in conjunction with a CGL policy.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.9 7. Representations and Warranties Insurance

§14.9 7. Representations and Warranties Insurance

Several companies now offer representations and warranties (R&W) insurance in connection with real estate transactions outside the mergers and acquisitions context. Like an errors and omissions policy, it is a stand-alone policy and is usually obtained in conjunction with a CGL policy. There is no standard-language R&W policy. The contract or agreement containing the subject representations and warranties is identified as the "R&W Contract." "R&W Loss" is defined as "a loss incurred by Insured that arises out of breach of the Reps & Warranties." Thus, R&W insurance is not limited to "property damage" or "bodily injury" or "personal and advertising injury" as are CGL and BOP policies. R&W insurance extends to the resulting financial losses if specifically identified representations and warranties are untrue. See §§14.76-14.79.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.10 8. Homeowners

§14.10 8. Homeowners

There are several commonly used versions of the ISO Homeowners policy: the Homeowners 3 Special Form (HO 00 03); the Broad Form (HO 00 02); and the Unit Owners Form (HO 00 06), which is used for condominiums. These forms differ principally in the property coverage each provides in Section I (see chap 13). Section II, which provides liability coverage, is virtually identical in each form. The Homeowners policies provide coverage for "bodily injury" (see §14.28) and "property damage" (see §14.25) caused by an "occurrence" (see §14.18). They do not provide "advertising injury" or "personal injury" (see §§14.69-14.70) coverage, as these are usually associated with commercial risks.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.11 D. Issues Arising Under Various Policies

§14.11 D. Issues Arising Under Various Policies

Just as there are too many types of policies to discuss in detail in one chapter, there are far too many issues that may arise under liability policies in connection with real estate transactions. The remaining sections in this chapter discuss how various insurance policy provisions may affect the availability of coverage for occurrences and claims commonly arising in real estate transactions.

© The Regents of the University of California

II. SPECIAL ISSUES: OCCURRENCE; CLAIMS MADE; AND CLAIMS MADE AND REPORTED POLICIES

§14.12 A. Occurrence Policies

Commercial General Liability policies, Businessowners policies, Owners and Contractors Protective Liability policies, and Homeowners policies typically require that "bodily injury" and "property damage" be caused by an "occurrence" during the policy period. This limitation is the chief distinction between an "occurrence-based" policy versus a "claims made" policy.

A typical "occurrence" policy, such as the standard form CGL policy, provides liability coverage for *damage or injury occurring during the policy period* that results from an accident, or from continuous or repeated exposure to injurious conditions. However, the sudden, accidental damage-causing act or event, or the conditions giving rise to the damage or injury, need not actually occur within the policy period in order for potential liability coverage to arise. *Montrose Chem. Corp. v Admiral Ins. Co.* (1995) 10 C4th 645, 675, 686, 42 CR2d 324. The occurrence of bodily injury or property damage during the policy period is the operative event that triggers coverage. 10 C4th at 668. Thus, the standard occurrence-based CGL policy provides coverage for injury or damage that may not be discovered or manifested until after the policy period expires (10 C4th at 689) and even if the claim is not made until long after the policy has expired. *Homestead Ins. Co. v American Empire Surplus Lines Ins. Co.* (1996) 44 CA4th 1297, 1303, 52 CR2d 268; *Pacific Employers Ins. Co. v Superior Court* (1990) 221 CA3d 1348, 1356, 270 CR 779. See the discussion of continuous or progressive loss in §14.48.

© The Regents of the University of California

§14.13 B. "Claims Made" Policies

In a "claims made" policy, "the carrier agrees to assume liability for any errors, including those made prior to the inception of the policy, as long as a claim is made during the policy period." *Homestead Ins. Co. v American Empire Surplus Lines Ins. Co.* (1996) 44 CA4th 1297, 1303, 52 CR2d 268. See also *World Health & Education Foundation v Carolina Cas. Ins. Co.* (ND Cal 2009) 612 F Supp 2d 1089, 1094 n1; *Westrec Marina Mgmt., Inc. v Arrowood Indem. Co.* (2008) 163 CA4th 1387, 1395, 78 CR3d 264; *Pacific Employers Ins. Co. v Superior Court* (1990) 221 CA3d 1348, 1356, 270 CR 779.

"Claims made" or "claims made and reported" coverage is typically found in professional liability policies (although the ISO Commercial General Liability Form (CG 00 02) is a "claims made" policy). For example, the Architects and Engineers Professional Liability policy (see §14.6), the Contractors Professional Liability policy (see §14.7), and the Representations and Warranties policy (see §§14.9, 14.76) are all "claims made" policies.

Under a "claims made" policy (*Homestead Ins. Co.,* 44 CA4th at 1304),

> [c]overage does not depend on when the actual or alleged negligent act, error or omission occurred, but on when the claim is made against the insured.… [T]he insurer generally is responsible for loss resulting from claims made during the policy period no matter when the liability-generating event took place.

See also *Pacific Employers Ins. Co.,* 221 CA3d at 1358.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.14 C. 'Claims Made and Reported' Policies

§14.14 C. "Claims Made and Reported" Policies

A third variation, the "claims made and reported" policy, requires that the claim be made and be reported to the insurer during the policy period. A "claims made" policy does not impose such a reporting requirement. See *Pension Trust Fund v Federal Ins. Co.* (9th Cir 2002) 307 F3d 944, 956.

© The Regents of the University of California

§14.14A D. What Is a "Claim"?

Although a "claim" is required to trigger coverage under either a "claims made" or a "claims made and reported" policy, there are surprisingly few reported appellate decisions defining what is and what is not a "claim."

A "claim," both in its ordinary meaning and in the interpretation given to it by the courts, is a demand for something as a right, or as due. *Westrec Marina Mgmt., Inc. v Arrowood Indem. Co.* (2008) 163 CA4th 1387, 1392, 78 CR3d 264; *Safeco Surplus Lines Co. v Employers' Reinsurance Corp.* (1992) 11 CA4th 1403, 1407, 15 CR2d 58; *Phoenix Ins. Co. v Sukut Constr. Co.* (1982) 136 CA3d 673, 677, 186 CR 513. Other cases define a "claim" as money demanded for a debt due the claimant (*Williamson & Vollmer Eng'g, Inc. v Sequoia Ins. Co.* (1976) 64 CA3d 261, 269, 134 CR 427) or the assertion of a liability of the party, demanding that the party perform some service or pay money. *Abifadel v Cigna Ins. Co*. (1992) 8 CA4th 145, 160, 9 CR2d 910; *Hill v Physicians & Surgeons Exch.* (1990) 225 CA3d 1, 6, 274 CR 702.

It seems accepted that a formal lawsuit is not required to constitute a "claim." *Abifadel,* 8 CA4th at 160; *Hill,* 225 CA3d at 6; *Phoenix Ins. Co.,* 136 CA3d at 677; *Williamson & Vollmer Eng'g, Inc.,* 64 CA3d at 270.

A request for an explanation is not a claim. *Abifadel,* 8 CA4th at 160; *Hill,* 225 CA3d at 5; *Mt. Hawley Ins. Co. v Federal Sav. & Loan Ins. Co.* (CD Cal 1987) 695 F Supp 469, 479. Further, an expression of dissatisfaction or disappointment, "mere complaining," or the lodging of a grievance without a demand for compensation is not a claim. *Westrec Marina Mgm't, Inc.,* 163 CA4th at 1392; *Abifadel,* 8 CA4th at 160; *Hill,* 225 CA3d at 5. At least one reported case held that threatened action, or a statement of intent to hold the insured responsible, is not a "claim." *Abifadel,* 8 CA4th at 161.

PRACTICE TIP: This seemingly simple definition has proven difficult to apply. When a threat of legal action or a statement of intent to hold the insured responsible crosses the line to become a demand for compensation is not clear. The court's decision as to whether a communication constitutes a "claim" will depend on the relationship of the parties and all the circumstances of the case.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.15 E. Extended Reporting Period

§14.15 E. Extended Reporting Period

An "extended reporting period" may be available under many "claims made" policies. An extended reporting period allows additional time, after the end of the policy period, for the insured to report a claim. See *Root v American Equity Specialty Ins. Co.* (2005) 130 CA4th 926, 933, 30 CR3d 631.

WARNING: An "extended reporting period" does not necessarily simply lengthen the policy period to a later date. The extended time to report a claim may not apply to a claim made during the original policy period, but rather is interpreted literally to claims made and reported, within the time specified by the policy, in the distinct extended reporting period. See *World Health & Education Foundation v Carolina Cas. Ins. Co.* (ND Cal 2009) 612 F Supp 2d 1089 (extended reporting period applicable to "any claim first made and reported during a period of 60 days after the date upon which the Policy Period ends," did not extend time to report claim made before policy period ended).

The extended reporting period may take effect automatically, as occurs when the policy is canceled or not renewed; this automatic extension is for a short term, often 60 days. 130 CA4th at 933. A longer extended reporting period, of 1 year or several years, may be available on payment of an additional premium.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.16 F. Retroactive Date

§14.16 F. Retroactive Date

"Claims made" policies typically contain a "retroactive date." The policy provides that the error or omission that gives rise to the claim must take place on or after the retroactive date. The application typically requires the insured to state, under oath, that they are not aware of any events that could give rise to a claim that occurred on or after the retroactive date.

© The Regents of the University of California

§14.17 III. SPECIAL ISSUES: COMMERCIAL GENERAL LIABILITY

The purpose of CGL policies is "to provide the insured with the broadest spectrum of protection against liability for unintentional and unexpected personal injury or property damage arising out of the conduct of the insured's business." *MacKinnon v Truck Ins. Exch.* (2003) 31 C4th 635, 654, 3 CR3d 228.

Under standard CGL policies, the insurer has a duty to indemnify the insured for sums that the insured becomes legally obligated to pay as damages for a covered claim. *Aerojet-General Corp. v Transport Indem. Co.* (1997) 17 C4th 38, 56, 70 CR2d 118; *Buss v Superior Court* (1997) 16 C4th 35, 45, 65 CR2d 366. By definition, this duty entails the payment of money, which is expressly limited in amount, in order to resolve liability. *Aerojet-General,* 17 C4th at 56; *Buss,* 16 C4th at 46. It is not narrowly confined to money that the insured must give under law as compensation to third parties, but may also include money that the insured must itself expend in equity in order to provide relief of the same sort. *Aerojet-General,* 17 C4th at 56; *AIU Ins. Co. v Superior Court* (1990) 51 C3d 807, 819, 274 CR 820. The duty to indemnify runs to claims that are actually covered, in light of the facts proved. See, *e.g., Aerojet-General,* 17 C4th at 56; *Buss,* 16 C4th at 46.

The insurer's duty to indemnify the insured arises only after liability is established and as a result of the liability. See, *e.g., Aerojet-General,* 17 C4th at 56; *Buss,* 16 C4th at 46; *Montrose Chem. Corp. v Admiral Ins. Co.* (1995) 10 C4th 645, 659 n9, 42 CR2d 324. The duty is triggered if specified harm is caused by an included occurrence, as long as at least some of the harm results within the policy period (*Aerojet-General,* 17 C4th at 56; *Montrose,* 10 C4th at 669), and extends to all specified harm caused by an included occurrence, even if some of the harm results beyond the policy period (see *Aerojet-General,* 17 C4th at 57). In other words, "an insurer on the risk when continuous or progressively deteriorating damage or injury first manifests itself remains obligated to indemnify the insured for the entirety of the ensuing damage or injury." *Montrose,* 10 C4th at 686.

Standard comprehensive or commercial general liability insurance policies also provide that the insurer has a duty to defend the insured in any action brought against the insured seeking damages for a covered claim. *Aerojet-General,* 17 C4th at 57; *Buss,* 16 C4th at 45. By definition, the duty entails the rendering of a service, *i.e.,* the mounting and funding of a defense (*Buss,* 16 C4th at 46), which is not limited, expressly or otherwise, in order to avoid or at least minimize liability. See *Aerojet-General,* 17 C4th at 58; *Gray v Zurich Ins. Co.* (1966) 65 C2d 263, 279, 54 CR 104. As such, it requires the undertaking of reasonable and necessary efforts for that purpose, including investigation. See *Aerojet-General,* 17 C4th at 58; *Pacific Indem. Co. v Universal Underwriters Ins. Co.* (1965) 232 CA2d 541, 543, 43 CR 26. The duty also requires the insurer to incur reasonable and necessary costs to that end, including investigative expenses. See *Aerojet-General,* 17 C4th at 58; *Pacific Indem. Co.,* 232 CA2d at 543. It runs to claims that are merely potentially covered, in light of facts alleged or otherwise disclosed, and arises as soon as tender is made (*Aerojet-General,* 17 C4th at 58; *Buss,* 16 C4th at 46), before liability is established and apart from it (*Aerojet-General,* 17 C4th at 58; *Montrose,* 10 C4th at 659 n9). It is discharged when the action is concluded and may be extinguished earlier if it is shown that no claim can in fact be covered. *Aerojet-General,* 17 C4th at 58; *Buss,* 16 C4th at 46. If it is so extinguished, however, it is extinguished only prospectively and not retroactively: Before, the insurer had a duty to defend; after, it does not have a duty to defend further. *Aerojet-General,* 17 C4th at 58; *Buss,* 16 C4th at 46. The duty to defend is triggered if specified harm may possibly have been caused by an included occurrence, so long as at least some such harm may possibly have resulted within the policy period, and extends to all specified harm that may possibly have been caused by an included occurrence, even if some such harm may possibly have resulted beyond the policy period. *Aerojet-General,* 17 C4th at 58. That is, if specified harm may possibly have been caused by an included occurrence and may possibly have resulted, at least in part, within the policy period, the duty to defend applies to all points in time at which any such harm may possibly have resulted after the policy period. *Aerojet-General,* 17 C4th at 58

© The Regents of the University of California

§14.18 A. "Occurrence" or "Accident"

An "occurrence" is typically defined as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions." ISO Form CG 00 01 12 04 (§V, ¶13), p 14.

Standard CGL policy language was revised by insurance industry drafters in several important respects starting in 1966. Before that year, third party general liability policies covered bodily injuries and damages caused by "accidents." In 1966, the National Bureau of Casualty Underwriters and the Mutual Insurance Rating Board, the predecessor organizations to the Insurance Services Office (ISO), changed the standard form policy from an "accident-based" to an "occurrence-based" format. See *Montrose Chem. Corp. v Admiral Ins. Co.* (1995) 10 C4th 645, 671, 42 CR2d 324 (*Montrose II*). Note that the terms "accident" and "occurrence" are not synonymous, because "occurrence" also includes "continuous or repeated exposure to substantially the same general harmful conditions." The change was made in order to clarify the insurer's intent with respect to time of coverage and application of policy limits, particularly in situations involving a related series of events attributable to the same factor. Under such circumstances, only one accident or occurrence is intended *insofar as the application of policy limits is concerned*.

EXAMPLE: If multiple freight cars are derailed in a collision with a contractor's equipment, the occurrence limit of the policy is intended to be applied only once for purposes of the contractor's liability. 10 C4th at 672.

There is little doubt that the definition of "occurrence" in the newly drafted standard form CGL policy was intended to provide coverage when damage or injury resulting from an accident or "injurious exposure to conditions" occurs during the policy period. The term "accident" was left in the definition of occurrence for the purpose of circumscribing the policy limits applicable to each occurrence. The drafters did not intend that an "accident" in the literal sense, *e.g.,* a sudden precipitating event, must occur during the policy period in order to trigger potential coverage for ensuing damage or injury.

> "The reference to 'injurious exposure to conditions [resulting in]… bodily injury [or property damage]' eliminates any requirement that the injury result from a sudden event. Although it is most common that an injury takes place simultaneously with the exposure, there are many instances of injuries taking place over an extended period of time before they become evident [for example, the slow ingestion of foreign substances or the inhalation of noxious fumes]. In these and similar cases, the definition of 'occurrence' identifies the time of loss for purposes of applying coverage—the injury must take place during the policy period."

Montrose Chem. Corp., 10 C4th at 672, quoting 3 Cal Insurance Law & Practice, Property and Liability Insurance §49.12, p 49-20 (1986). See also the discussion of continuous or progressive loss in §14.48.

The term "accident" is not defined in either the ISO Businessowners Coverage Form (BP 00 03 07 02) or the ISO CGL Policy (CG 00 01 12 04). There is no all-inclusive definition of "accident." Nevertheless, in the context of liability insurance coverage, the California Supreme Court has defined an "accident" as "an unexpected, unforeseen, or undesigned happening or consequence from either a known or an unknown cause.… This common law construction of the term 'accident' becomes part of the policy and precludes any assertion that the term is ambiguous." *Delgado v Interins. Exch. of the Auto. Club of S. Cal.* (2009) 47 C4th 302, 308, 97 CR3d 298 (citations omitted).

In *Delgado,* the Supreme Court held that, "an insured's unreasonable belief in the need for self-defense does not turn the resulting purposeful and intentional act of assault and battery into 'an accident.'" 47 C4th 302 at 317. The word "accident" in the coverage clause of a liability policy refers to the conduct of the insured for which liability is sought to be imposed on the insured. In other words, "a purposeful and intentional act remains purposeful and intentional regardless of the insured's reason or motivation for it." 47 C4th at 314. An injury-producing event is not an "accident" within a liability policy's coverage language if all of the acts, the manner in which they were done, and the objective accomplished occurred as the actor intended. *Delgado*, at 311 (citing authorities).

© The Regents of the University of California

§14.19 1. "Accidental" and "Negligent" Not Synonymous

It is commonly argued that if the underlying complaint alleges negligence, there must be a duty to defend. This is not necessarily true: "Negligent" and "accidental" are not synonymous. *Quan v Truck Ins. Exch.* (1998) 67 CA4th 583, 596, 79 CR2d 134; *American Int'l Bank v Fidelity & Deposit Co.* (1996) 49 CA4th 1558, 1573, 57 CR2d 567. The argument that an allegation of negligence gives rise to a duty to defend misconstrues the "accident" requirement in standard general liability policies. Under California law, the term "accident" refers to "the nature of the insured's conduct, not his state of mind." *Collin v American Empire Ins. Co.* (1994) 21 CA4th 787, 804, 26 CR2d 391. Even when conduct is alleged to be "negligent" because the insured did not intend any harm, no duty to defend will arise if the conduct could not be engaged in "by accident." *Quan v Truck Ins. Exch.,* 67 CA4th at 595 (insured's allegedly negligent conduct in serving alcohol to minor, or belief that victim consented, not "accidental" because there was no potential under circumstances for accidental sexual assault); *Ulrich v State Farm Fire & Cas. Co.* (2003) 109 CA4th 598, 611, 135 CR2d 131 (extrinsic facts demonstrated alleged assault, wrongful detention, and defamation, which could not have been committed "by accident").

© The Regents of the University of California

§14.20 a. Examples of "Accidental" Conduct

The following cases illustrate conduct held to be "accidental":

- Negligent design or construction: *Baugh Constr. Co. v Mission Ins. Co.* (9th Cir 1988) 836 F2d 1164, 1169; *Pepperell v Scottsdale Ins. Co.* (1998) 62 CA4th 1045, 73 CR2d 164.
- Negligent design and maintenance: *Stonewall Ins. Co. v City of Palos Verdes Estates* (1996) 46 CA4th 1810, 54 CR2d 176.
- Architect's approval of inferior materials that cause construction of a defective building: *Gogerty v General Acc., Fire & Life Assur. Corp.* (1965) 238 CA2d 574, 48 CR 37.
- Default on contractual obligations: *Business to Business Markets, Inc. v Zurich Specialties London Ltd.* (2005) 135 CA4th 165, 37 CR3d 295.
- Self defense: *Jafari v EMC Ins. Cos.* (review granted Dec. 12, 2007, S157924; superseded opinion at 155 CA4th 885, 66 CR3d 359. Further action on the matter deferred pending consideration and disposition of related issues in *Delgado v Interins. Exch. of the Auto. Club of S. Cal.* (2009) 47 C4th 302, 308, 97 CR3d 298. Injuries inflicted by insured's employee defending against customer may be "accidental" conduct requiring coverage.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.21 b. Examples of Non-'Accidental' Conduct

§14.21 b. Examples of Non-"Accidental" Conduct

The following cases illustrate conduct held to be not "accidental":

- Bad professional advice rendered by a roofing contractor: *Ray v Valley Forge Ins. Co.* (1999) 77 CA4th 1039, 92 CR2d 473.
- Property destroyed by intentional acts of the insured, such as arson or demolition for renovation: See *Home Sav. v Continental Ins. Co.* (2001) 87 CA4th 835, 848, 104 CR2d 790.
- Incomplete renovation work approved by the mortgagee: *Wilson v Farmers Ins. Exch.* (2002) 102 CA4th 1171, 126 CR2d 305.
- Negligent or intentional misrepresentation and failure to disclose defects in home sold by insured: *Miller v Western General Agency, Inc.* (1996) 41 CA4th 1144, 49 CR2d 55.
- Wrongful eviction: *Swain v California Cas. Ins. Co.* (2002) 99 CA4th 1, 8, 120 CR2d 808.

© The Regents of the University of California

§14.22 2. Failure to Disclose; Misrepresentations Upon Sale

Claims for negligent or intentional misrepresentation or concealment that do not include property damage or damage to tangible property are not covered by a liability policy. In *Miller v Western General Agency, Inc.* (1996) 41 CA4th 1144, 49 CR2d 55, for example, the insureds sold their home without disclosing that the foundation was settling, that the home had various leaks, or that the home had inadequate or defective electrical wiring. The buyer sued, alleging negligent and intentional misrepresentation or concealment of the condition of the home. The court held that their claims did not allege "accidental conduct," did not seek "property damage" or damage to tangible property, and fell within the exclusion for damages that may be expected or intended from the standpoint of the insured.

Similarly, in *Devin v United Servs. Auto. Ass'n* (1992) 6 CA4th 1149, 1158, 8 CR2d 263, the court held that the allegation that the insureds failed to disclose that a house was "sliding, slipping, settling, sinking, fracturing and buckling" was an allegation that the plaintiff caused a "pecuniary loss"—the loss of the fair market value of the home—that did not constitute "property damage."

© The Regents of the University of California

§14.23 3. Latent Defects

Concealed or "latent" defects are those that are not apparent during a reasonable inspection of the property. If they are caused by the insured's negligent design or construction, they may cause covered "property damage" during a CGL policy term. This may be true even when the policies extending coverage to the insured have expired before a third party purchaser discovers the damage. *Century Indem. Co. v Hearrean* (2002) 98 CA4th 734, 740, 120 CR2d 66 (concealed defects consisted of negligent design and construction, causing leaking windows, roofs, and cracked exterior stucco). See the discussion of continuous or progressive loss in §14.48.

© The Regents of the University of California

§14.24 4. Negligent Construction; Negligent Design

Standard CGL policies contain an exclusion stating that the policy does not apply "to that particular part of any property, not on premises owned by or rented to the insured… the restoration, repair or replacement of which has been made or is necessary by reason of faulty workmanship thereon by or on behalf of the insured." See *George F. Hillenbrand, Inc. v Insurance Co. of N. Am.* (2002) 104 CA4th 784, 793, 128 CR2d 586. By implication, CGL policies therefore cover (1) damage to the building if it resulted from some cause other than the contractor's own faulty workmanship, *e.g.,* improper maintenance by others, defective materials, or design; or (2) damage to property (other than the insured's work) caused by the insured's faulty workmanship. 104 CA4th at 794. The courts do not look to see whether noncovered acts predominate in the third party's action, but rather to whether there is any potential for liability under the policy. 104 CA4th at 801.

In *Marquez Knolls Prop. Owners Ass'n v Executive Risk Mgmt., Inc.* (2007) 153 CA4th 228, 62 CR3d 510, a homeowners association ruled that a member's enclosed patio structure violated its covenants, conditions, and restrictions (CC&Rs). The homeowner sued the association. The association's insurer denied coverage, relying on an exclusion for claims in any way involving "the design, construction, renovation or rehabilitation of any building, structure, or other improvement on any real property." The court held the exclusion did not apply because it relates only to the insured association's design, construction, renovation, or rehabilitation of improvements, and not to those of the individual homeowner.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.25 B. Property Damage; Defective or Faulty Materials

§14.25 B. Property Damage; Defective or Faulty Materials

Commercial general liability policies were formerly called "comprehensive general liability" policies and both are known as "CGL" policies. CGL and homeowner liability insurance policies were amended in the 1970s to eliminate coverage for economic damages.

> Prior to 1973, the standard CGL policy defined "property damage" as "injury to or destruction of tangible property." Applying that definition, a number of courts held that coverage for "property damage" included the diminution in the value of the building resulting from incorporation of a defective component. Beginning in 1973, the definition of "property damage" in the standard CGL policy was changed to "physical injury to or destruction of tangible property." Giving this new definition its plain and ordinary meaning, the majority of courts hold that [the addition of the word "physical" eliminates coverage for] economic damages.

F & H Constr. v ITT Hartford Ins. Co. (2004) 118 CA4th 364, 374, 12 CR3d 896. See the discussion of defective or faulty materials in §§14.26-14.27.

The 2004 CGL form defines "property damage" as "[p]hysical injury to tangible property, including all resulting loss of use of that property" and "[l]oss of use of tangible property that is not physically injured." CG 00 01 12 04 (§V, ¶17), p 14.

"Tangible property" is not ambiguous, and coverage therefore does not turn on alternative meanings. Consistent with an insured's reasonable expectations, "'tangible property' refers to things that can be touched, seen, and smelled." *Kazi v State Farm Fire & Cas. Co.* (2000) 24 C4th 871, 880, 103 CR2d 1; *Warner v Fire Ins. Exch.* (1991) 230 CA3d 1029, 1034, 281 CR 635.

The property loss section of the standard liability policy provides coverage for "physical injury or destruction of tangible property" that occurs during the policy term. The focus of coverage for property damage is therefore the property itself, and does not include intangible economic losses, violation of antitrust laws, or nonperformance of contractual obligations. Strictly economic losses—like lost profits, loss of goodwill, loss of the anticipated benefit of a bargain, and loss of an investment—do not constitute damage or injury to tangible property covered by a CGL policy. *Waller v Truck Ins. Exch.* (1995) 11 C4th 1, 17, 44 CR2d 370. See also *Golden Eagle Ins. Corp. v Cen-Fed, Ltd.* (2007) 148 CA4th 976, 987, 56 CR3d 279. Additional examples include:

- Contractor's welding of subcontractor's inadequate pile caps to its driven steel piles did not constitute property damage under CGL policy, which had been issued to subcontractor; damages alleged by contractor arising from subcontractor's provision of inadequate caps only listed costs of modifying pile caps to conform to contractual specifications and lost bonus for early completion of construction project, which damages were intangible economic damages rather than damages to tangible property. *F&H Constr. v ITT Hartford Ins. Co., supra*.
- Landlord's alleged failure to timely deliver the real property to the tenant for use as an automobile dealership did not cause a loss of use of the vehicles and, therefore, did not cause "property damage" within the meaning of landlord's CGL insurance policy; the landlord at most caused economic damage. *Cunningham v Universal Underwriters* (2002) 98 CA4th 1141, 120 CR2d 162.
- Investors' physical and emotional distress deriving from their investment loss, which was negligently inflicted upon them by directors and officers of insured, did not come within property damage coverage under CGL policy; damage for lost profits, loss of investment, or other harm to one's economic interest constituted injuries to intangible property that by definition fell outside scope of policy. *McLaughlin v National Union Fire Ins. Co.* (1994) 23 CA4th 1132, 29 CR2d 559.
- Economic damages resulting to buyers from sellers' negligent misrepresentation about size of lot was not damage to "tangible property" within coverage for third party claims under sellers' all-risk homeowner's policy. *Warner v Fire Ins. Exch.* (1991) 230 CA3d 1029, 281 CR 635.
- Diminution in value of a lease due to the landlord's failure to maintain the premises as required in the lease did not constitute "physical injury to tangible property" under landlord's liability policy. *Golden Eagle Ins. Corp. v Cen-Fed, Ltd.* (2007) 148 CA4th 976, 987, 56 CR3d 279.

© The Regents of the University of California

§14.25A 1. Damages

In *Certain Underwriters at Lloyd's of London v Superior Court* (2001) 24 C4th 945, 961, 103 CR2d 672 *(Powerine I)*, the supreme court held that the insurer's duty to indemnify was limited to "damages, *i.e.*, money ordered by a court." The court held that administrative orders directing a defunct oil company to clean up contaminated sites were not "damages."

In *Powerine Oil Co., Inc. v Superior Court* (2005) 37 C4th 377, 33 CR3d 562 *(Powerine II),* the excess insurer's policy required it to indemnify for damages and expenses, "all as more fully defined by the term 'ultimate net loss'." "Ultimate net loss" was defined as the total sum the insured became obligated to pay "either through adjudication or compromise, and shall also include… expenses… for litigation, settlement, adjustment and investigation of claims and suits." 37 C4th at 395. The court held that this broader language obligated the insurer to indemnify the insured's costs arising from an administrative clean-up order.

In contrast, in *County of San Diego v Ace Prop. & Cas. Ins. Co.* (2005) 37 C4th 406, 416, 33 CR3d 583, the excess policy required the insurer to indemnify the insured "'for all sums which the insured is obligated to pay by reason of liability imposed by law or assumed under contract or agreement,' arising from 'damages' caused by personal injuries or the destruction or loss of use of tangible property." 37 C4th at 411. The court held that this language in the excess policy, like the insuring language in the standard ISO CGL policy, does not apply to settlement costs agreed to with third parties outside the context of a court suit.

In *Aerojet-General Corp. v Commercial Union Ins. Co.* (2007) 155 CA4th 132, 65 CR3d 803, the excess policies required the insurers to pay "all sums which the assured shall become legally obligated to pay, or by any final judgment be adjudged to pay, to any person or persons as damages." 155 CA4th at 143. The appellate court held that costs incurred to remediate polluted property under a settlement in a separate legal action were not "damages" because the settlement agreement was negotiated by the insured and did not involve a court order or judgment.

PRACTICE TIP: The *Aerojet-General* court rejected the insured's argument that the insurer was equitably estopped from refusing to pay the settlement because the insured kept the insurer apprised of its settlement strategies and negotiations and reasonably relied on the insurer to voice any concerns or objections. The court noted that the insurer refused to participate in any settlement negotiations and had reserved the right to contest coverage. Perhaps even more important, the insured's counsel wrote a letter proposing that the settlement agreement be entered as a stipulated judgment, in order to "protect against their insurers in light of" *Powerine I*. Counsel for insureds whose policies contain language such as that found in *Powerine I* or *Aerojet-General* should be sure to get the insurer to waive, in writing, any defense based on the definition of "damages," or have any settlement reduced to a judgment.

© The Regents of the University of California

§14.26 2. Physical Injury to Other Property

Standard CGL policies define "property damage" as "[p]hysical injury to tangible property, including all resulting loss of use of that property" and "[l]oss of use of tangible property that is not physically injured." *F & H Constr. v ITT Hartford Ins. Co.* (2004) 118 CA4th 364, 371, 12 CR3d 896. Courts applying standard CGL policy language generally agree that the incorporation of a defective component or product into a larger structure or system does not constitute physical injury to tangible property, unless and until the defective component physically injures some other tangible part of the larger system or the system as a whole. 118 CA4th at 372. In other words, the mere presence of a defective part causing no immediate harm does not produce physical injury. 118 CA4th at 372. See, *e.g*., *Hogan v Midland Nat'l Ins. Co.* (1970) 3 C3d 553, 91 CR 153 (defective saw leading to improperly cut lumber); *Geddes & Smith, Inc. v St. Paul Mercury Indem. Co.* (1959) 51 C2d 558, 563, 334 P2d 881 (defective doors sent to contractor; installation caused damage to third parties); *Economy Lumber Co. v Insurance Co. of N. Am.* (1984) 157 CA3d 641, 204 CR 135 (defective siding sent to contractor and caused damage). A contractor's removal of the defective items, which unavoidably caused additional damage, was covered under the supplier's liability policy. *Economy Lumber Co.,* 157 CA3d at 651.

Further, when products or work containing hazardous materials have been incorporated into other products or structures, courts have found immediate harm and physical injury to other property at the moment the incorporation occurred. *Watts Indus., Inc. v Zurich Am. Ins. Co.* (2004) 121 CA4th 1029, 1044, 18 CR3d 61 (metallurgically substandard parts incorporated into water system, causing contamination of water and damage to water system, was alleged to be "property damage," and insurer had duty to defend because parts could not easily be removed); *Shade Foods, Inc. v Innovative Prods. Sales & Mktg., Inc.* (2000) 78 CA4th 847, 865, 93 CR2d 364 (ingredient containing wood splinters incorporated into food product); *World Indus., Inc. v Aetna Cas. & Sur. Co.* (1996) 45 CA4th 1, 90, 52 CR2d 690.

© The Regents of the University of California

§14.27 3. No Physical Injury to Other Property

Incorporation of a defective component or product into a larger structure does not constitute property damage unless and until the defective component causes physical injury to tangible property in at least some other part of the system. *F & H Constr. v ITT Hartford Ins. Co.* (2004) 118 CA4th 364, 372, 12 CR3d 896; *St. Paul Fire & Marine Ins. Co. v Coss* (1978) 80 CA3d 888, 892, 145 CR 836 (defective materials and workmanship in construction of home not physical injury); *New Hampshire Ins. Co. v Vieira* (9th Cir 1991) 930 F2d 696 (faulty installation of drywall into building not physical injury); *Esicorp, Inc. v Liberty Mut. Ins. Co.* (8th Cir 2001) 266 F3d 859, 863 (defective steel pipe sections welded into pipe system not physical injury).

Under these cases, property damage is not established by the mere failure of a defective product to perform as intended; nor is it established by economic losses, such as the diminution in value of the structure (*New Hampshire Ins. Co.,* 930 F2d at 700) or the cost to repair a defective product or structure (*F & H Constr.,* 118 CA4th at 372; *New Hampshire Ins. Co.,* 930 F2d at 700).

© The Regents of the University of California

§14.28 C. Bodily Injury

Current ISO forms define "bodily injury" as "bodily injury, sickness or disease sustained by a person, including death resulting from any of these at any time" (CG 00 01 12 04 (§V, ¶3), p 12; BP 00 03 07 02 (§II.F, ¶3), p 37), or "bodily harm, sickness or disease, including required care, loss of services and death that results" (HO 00 03 10 90 (Definitions, ¶B.2), p 1).

© The Regents of the University of California

§14.29 1. Emotional Distress Without Physical Injury

"Pure" emotional distress, unaccompanied by any physical injury or manifestations, is not "bodily injury." For example, in *Aim Ins. Co. v Culcasi* (1991) 229 CA3d 209, 219, 280 CR 766, the court held that the "critical word in the term 'bodily injury' is 'bodily.'" After citing several dictionary definitions of the word "bodily," which drew a distinction between the physical, corporeal body versus mental or spiritual condition, the court concluded that "the ordinary and popular meaning of the word 'bodily' does not reasonably encompass, and in fact suggests a contrast with, the purely mental, emotional, and spiritual." 229 CA4th at 219. The court held that claims for emotional distress, without physical injury or manifestation, did not constitute "bodily injury." 229 CA4th at 227; see also *Chatton v National Union Fire Ins. Co.* (1992) 10 CA4th 846, 854, 13 CR2d 318 ("the phrase 'bodily injury, sickness or disease' is plain and unambiguous and coverage under the bodily injury clause is limited to physical injury to the body and does not include nonphysical, emotional or mental harm."); *Mercury Ins. Co. v Ayala* (2004) 116 CA4th 1198, 1204, 11 CR3d 158 (same).

The supreme court held that CGL policies do not provide coverage for economic losses that cause emotional distress. *Waller v Truck Ins. Exch.* (1995) 11 C4th 1, 44 CR2d 370. The court stated that the policies "were never intended to cover emotional distress damages that flow from an uncovered 'occurrence,' and the parties could not reasonably have expected that coverage would be expanded merely because a claim of emotional or physical distress is alleged as a result of the economic loss." 11 C4th at 23; see also *Miller v Western General Agency, Inc.* (1996) 41 CA4th 1144, 1151, 49 CR2d 55 (emotional distress caused by misrepresentation and concealment of defective plumbing when insureds sold their home did not constitute "bodily injury").

© The Regents of the University of California

§14.30 2. Emotional Distress With Physical Injury

A more difficult issue involves whether physical manifestations of emotional distress, or emotional distress caused by physical injury, constitutes "bodily injury." In *Waller v Truck Ins. Exch.* (1995) 11 C4th 1, 40, 44 CR2d 370, in a concurring and dissenting opinion, Justice Kennard noted that

> [m]ost of the courts that have addressed the issue have held that any physical manifestations accompanying emotional distress are "bodily injuries" as that term is used in insurance policies. [Citations.] On its face, the policy's definitional language, "bodily injury, sickness, or disease," broadly covers any somatic condition, and does not exclude those that are caused or accompanied by mental distress.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.31 D. Insured Parties

§14.31 D. Insured Parties

Most policies contain a separate section on, or at least a definition of, who qualifies as an insured under the policy. This may include "named insureds" (see §§14.32-14.35), "additional named insureds" (see §14.36), and "additional insureds" (sometimes called "omnibus insureds"; see §§14.37-14.46).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.32 1. Named Insured; Additional Insured Distinguished

§14.32 1. Named Insured; Additional Insured Distinguished

The person indemnified under an insurance policy is the "insured." Ins C §23. The party purchasing the insurance is typically listed in the declarations for the policy as the "named insured." For definition of "who is the insured," see policy language quoted in §14.37. However, most liability policies extend coverage not only to the person or entity expressly listed on the policy, but also to other classes of additional insureds. See §14.37. The "named insured" is the person(s) or entity(ies) listed on the declarations page for the policy. *Fidelity & Deposit Co. v Charter Oak Fire Ins. Co.* (1998) 66 CA4th 1080, 1086, 78 CR2d 429.

> In contrast to a "named insured," an "additional insured" or "omnibus insured" is one who falls within the policy's omnibus definition of insureds, which typically includes employees, real estate managers, and third party beneficiaries. [Citation.] The names of "additional insureds" do not appear in the policy and the insurer typically does not even know who these persons are until a claim is filed.… "Additional named insureds" generally are persons who are added as insureds after the policy issues.

Kotlar v Hartford Fire Ins. Co. (2000) 83 CA4th 1116, 1121 n3, 100 CR2d 246. An additional named insured may be added in the policy declarations or by endorsement. See §14.36. See also §14.37 on additional insureds.

NOTE: Whether a party is an "additional insured" or an "additional named insured" should not affect the scope of the coverage afforded. However, an "additional insured" is not entitled to notice of cancellation under Ins C §677.2, but all named insureds, including all "additional named insureds," are entitled to notice of cancellation. *Kotlar,* 83 CA4th at 1121 n3.

© The Regents of the University of California

§14.33 a. Fictitious Names

Sole proprietors doing business under a fictitious name often, unfortunately, obtain policies listing their "dba" as the named insured. However, an insured must be a legal person, such as an individual, partnership, or corporation. Ins C §151; *Providence Washington Ins. Co. v Valley Forge Ins. Co.* (1996) 42 CA4th 1194, 1200, 50 CR2d 192. "The designation 'd/b/a' means 'doing business as' but is merely descriptive of the person or corporation who does business under some other name. Doing business under another name does not create an entity distinct from the person operating the business." 42 CA4th at 1200; see also Bus & P C §§17900-17930 (regulating fictitious business names). If the policy lists a "dba" as the named insured because of a mistake by the insured and the insurer, the policy may be reformed, or interpreted as if the individual sole proprietor was the named insured. 42 CA4th at 1200.

© The Regents of the University of California

§14.34 b. Partnerships

If a CGL or BOP policy is issued to a partnership, the individual partners and their spouses will be additional insureds, "but only with respect to the conduct of your business." See, *e.g.,* policy language quoted in §14.37. Many times, individual partners will be named as defendants in a lawsuit against the partnership. To avoid any dispute about whether the individual partners are sued "with respect to the conduct" of the business, partnerships will often list each individual partner as an additional named insured.

However, in *Milazo v Gulf Ins. Co.* (1990) 224 CA3d 1528, 274 CR 632, the CGL policy listed the named insured as each partner "dba" the partnership. The court held that the policy insured the partnership and the individual partners only with respect to their liability as partners, and not as individuals. 224 CA3d at 1536.

PRACTICE TIP: In the opening sentence of the *Milazo* opinion, the court described the party seeking coverage as "a duplicitous partner [who] seeks to obtain indemnification under a partnership liability policy for the damages caused to his innocent copartners by his misappropriation of a partnership opportunity." 224 CA3d at 1531. When partners are sued along with a partnership, the distinction between the partners' individual capacities and their liability as partners will seldom be an issue. However, the "belt and suspenders" approach is to seek a policy that names the partnership and each individual partner as named insureds, without any qualification as to their capacity or whether they are "dba" the partnership.

© The Regents of the University of California

§14.35 c. "The Insured," "An Insured," or "Any Insured"

Exclusions may refer to "the insured," "an insured," or "any insured." Typically, "the insured" is interpreted to refer to the named insured, but "an insured" or "any insured" means any insured or additional insured. *State Farm Mut. Auto. Ins. Co. v Jacober* (1973) 10 C3d 193, 207, 110 CR 1 (exclusion regarding bodily injury to "the insured" held ambiguous). For example, an exclusion for intentional acts of "the insured" excludes coverage only for the intentional acts of the named insured, but an exclusion for intentional acts of "an insured" excludes coverage for the intentional acts of any insured. *Western Mut. Ins. Co. v Yamamoto* (1994) 29 CA4th 1474, 35 CR2d 698; *Fire Ins. Exch. v Altieri* (1991) 235 CA3d 1352, 1360, 1 CR2d 360.

© The Regents of the University of California

§14.36 2. Additional Named Insureds

"Additional named insureds" generally are persons who are added as insureds after the policy issues. *Kotlar v Hartford Fire Ins. Co.* (2000) 83 CA4th 1116, 1121 n3, 100 CR2d 246. An additional named insured may be added in the policy declarations or by endorsement. See §§14.31-14.32.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.37 3. Additional Insureds

§14.37 3. Additional Insureds

Construction contracts and agreements collateral to real property sales in the due diligence phases often require one party to obtain liability insurance naming the other party as an "additional insured." In contrast to a "named insured," an "additional insured" or "omnibus insured" is one who falls within the policy's omnibus definition of insureds, which typically includes employees, real estate managers, and third party beneficiaries. The names of "additional insureds" do not appear in the policy and the insurer typically does not even know who these persons are until a claim is filed.

PRACTICE TIP: Consequently, under some agreements, the party who must procure the insurance is required to obtain an "additional insured endorsement" (see forms described in §14.42) or have the other party listed as an "additional named insured" (see §14.36). See Note in §14.32.

Most CGL policy forms generally define additional insureds (omnibus insureds) through the following language (ISO Form CG 00 01 12 04 (§II), p 8):

> SECTION II—WHO IS AN INSURED
> 1. If you are designated in the Declarations as:
> a. An individual, you and your spouse are insureds, but only with respect to the conduct of a business of which you are the sole owner.
> b. A partnership or joint venture, you are an insured. Your members, your partners, and their spouses are also insureds, but only with respect to the conduct of your business.
> c. A limited liability company, you are an insured. Your members are also insureds, but only with respect to the conduct of your business. Your managers are insureds, but only with respect to their duties as your managers.
> d. An organization other than a partnership, joint venture or limited liability company, you are an insured. Your "executive officers" and directors are insureds, but only with respect to their duties as your officers or directors. Your stockholders are also insureds, but only with respect to their liability as stockholders.
> e. A trust, you are an insured. Your trustees are also insureds, but only with respect to their duties as trustees.
> 2. Each of the following is also an insured:
> a. Your "volunteer workers" only while performing duties related to the conduct of your business, or your employees", other than either your "executive officers" (if you are an organization other than a partnership, joint venture or limited liability company) or your managers (if you are a limited liability company), but only for acts within the scope of their employment by you or while performing duties related to the conduct of your business. However, none of these "employees" or "volunteer workers" are insureds for:
> ….
> (2) "Property damage" to property:
> (a) Owned, occupied or used by,
> (b) Rented to, in the care, custody or control of, or over which physical control is being exercised for any purpose by you, any of your "employees", "volunteer workers", any partner or member (if you are a partnership or joint venture), or any member (if you are a limited liability company).
> b. Any person (other than your "employee" or "volunteer worker"), or any organization while acting as your real estate manager.

The 2002 Businessowners Coverage Form (BP 00 03 07 02 (§II.C), p 34) contains nearly identical language. However, unlike the Businessowners form, the CGL form includes as an additional insured newly acquired organizations, through the following language (ISO CG 00 01 12 04 (§II, ¶3), p 9):

> 3. Any organization you newly acquire or form, other than a partnership, joint venture or limited liability company, and over which you maintain ownership or majority interest, will qualify as a Named Insured if there is no other similar insurance available to that organization. However:
> a. Coverage under this provision is afforded only until the 90th day after you acquire or form the organization or the end of the policy period, whichever is earlier;
> b. Coverage A does not apply to "bodily injury" or "property damage" that occurred before you acquired or formed the organization; and
> c. Coverage B does not apply to "personal and advertising injury" arising out of an offense committed

before you acquired or formed the organization.

No person or organization is an insured with respect to the conduct of any current or past partnership, joint venture or limited liability company that is not shown as a Named Insured in the Declarations.

The rights of a named insured under an insurance policy "inure to all additional insureds under that policy." *National Auto. & Cas. Ins. Co. v California Cas. Ins. Co.* (1983) 139 CA3d 336, 341, 188 CR 670. Although many statutory provisions, such as those governing cancellation and notice of cancellation of auto or commercial policies, limit that general proposition (an "additional insured" is not entitled to notice of cancellation under Ins C §677.2, but all named insureds, including all "additional named insureds," are entitled to notice of cancellation; see *Kotlar v Hartford Fire Ins. Co.* (2000) 83 CA4th 1116, 1121 n3, 100 CR2d 246), an additional insured is entitled to defense and indemnity like a named insured.

To establish that it has no duty to defend, an insurer has the burden to either negate an element of the cause of action or show that the additional insured could not establish the duty to defend. *Frontier Oil Corp. v RLI Ins. Co.* (2007) 153 CA4th 1436, 63 CR3d 816 (involving a joint venturer additional insured and liability alleged not to have arisen from joint venture activities).

© The Regents of the University of California

§14.38 a. Sole Negligence

All additional insured endorsements cover claims against the additional insured based on vicarious liability for the named insured's negligence. Whether the endorsement also covers claims against the additional insured for its own negligence depends on the language of the endorsement.

With some exceptions, CC §2782(a) invalidates provisions in construction contracts that indemnify against liability for death, bodily injury, or injury to property "arising from the sole negligence or willful misconduct of the promisee…." However, §2782(a) expressly "does not affect the validity of any insurance contract…." Thus, a construction contract can require a contractor or subcontractor to obtain an additional insured endorsement that covers damages caused by the "sole negligence" of the additional insured. *American Cas. Co. v General Star Indem. Co.* (2005) 125 CA4th 1510, 1524, 24 CR3d 34. This is true even though (1) §2782 would preclude enforcement of the contractual indemnity promise made by the indemnitor, or (2) under the facts of the case and the terms of the contract of indemnity, the indemnitor had no obligation to provide indemnity to the indemnitee. 125 CA4th at 1525. Indeed, unless the insurance policy or the additional insured endorsement provides otherwise, the additional insured is covered for liability resulting from its own negligence as well as vicarious liability for the named insured's negligence. 125 CA4th at 1524.

Insurance companies are free to, and commonly do, issue additional insured endorsements that specifically limit coverage to situations in which the additional insured is faced with vicarious liability for negligent conduct by the named insured. Examples of such endorsement language include:

- Additional insured covered "only with respect to acts or omissions of the named insured" (*Consolidation Coal Co. v Liberty Mut. Ins.* (WD Pa 1976) 406 F Supp 1292, 1294 n2); *Monticello Ins. Co. v Essex Ins. Co.* (2008) 162 CA4th 1376, 1379, 76 CR3d 848;
- Additional insureds covered "only to the extent of liability resulting from occurrences arising out of negligence" of the named insured (*Harbor Ins. Co. v Lewis* (ED Pa 1983) 562 F Supp 800, 802);
- Additional insured covered "only to the extent [the additional insured] is held liable for [the named insured's] acts or omissions arising out of and in the course of operations" (*Maryland Cas. Co. v Nationwide Ins. Co.* (1998) 65 CA4th 21, 28, 76 CR2d 113);
- "This insurance does not apply to 'bodily injury' or 'property damage' arising out of the sole negligence or willful misconduct of, or for defects in design furnished by, [the additional insured]" (*Presley Homes, Inc. v American States Ins. Co.* (2001) 90 CA4th 571, 573, 108 CR2d 686).

© The Regents of the University of California

§14.39 b. Does Duty to Defend Extend to Entire Action?

Although the insurer may restrict its duty to indemnify an additional insured to claims against the additional insured based on vicarious liability for the named insured's negligence, these restrictions do not narrow the insurer's duty to defend. This is because in a "mixed action," if some claims are covered and some are not, the duty to defend extends to the entire action. *Buss v Superior Court* (1997) 16 C4th 35, 48, 65 CR2d 366. For further discussion of the duty to defend, see §§14.52-14.56.

For example, in *Presley Homes, Inc. v American States Ins. Co.* (2001) 90 CA4th 571, 108 CR2d 686, the policy issued to a subcontractor as the named insured included an endorsement that amended the definition of "insured" to specifically include the plaintiff, a real estate developer, subject to the following provisions (90 CA4th at 573):

> 1. This insurance applies only with respect to liability: [¶] a. Arising out of 'your work' for that insured by or for you; or [¶] b. Arising from the general supervision of 'your work' by [the additional insured]. [¶] 2. This insurance does not apply to 'bodily injury' or 'property damage' arising out of the sole negligence or willful misconduct of, or for defects in design furnished by, [the additional insured].

The insurer argued that this language meant its defense of the developer could be limited to defense regarding claims attributable to the subcontractor's work. The court held that although the endorsements limited the coverage for the developer to liability arising from the subcontractor's work, nothing in either the policies or the endorsements limited the insurer's obligation to provide the developer with a defense. 90 CA4th at 575.

However, in *Monticello Ins. Co. v Essex Ins. Co.* (2008) 162 CA4th 1376, 76 CR3d 848, the named insured was a drywall subcontractor. An endorsement made the general contractor an additional insured, "but only as respects negligent acts or omissions of the Named Insured." The policy also stated that "[i]t is further agreed that where no coverage shall apply herein for the Named Insured, no coverage nor defense shall be afforded to the above-identified additional insured." 162 CA4th at 1386 n4. Because the underlying complaint did not allege any defects in the drywall, the court held that there was no potential coverage for the named insured and, thus, no duty to defend the additional insured. 162 CA4th at 1387.

NOTE: It is difficult to reconcile the holdings in *Presley Homes* and *Monticello*. Notably, the *Monticello* court did not cite any cases dealing with the scope of the duty to defend an additional insured. It may be that courts will follow *Monticello* if the policy's additional insured provision expressly and unambiguously states that the duty to defend does not extend "where no coverage applies to the named insured." However, it appears that further case law, and perhaps a decision from the California Supreme Court, is needed to clarify this issue.

© The Regents of the University of California

§14.40 c. Statutory Limit on Indemnity Provisions

A 2005 amendment to CC §2782(c) provides that an indemnification provision, including cost to defend, in a residential construction contract or an amendment entered into after January 1, 2006, by which a subcontractor must indemnify a builder for construction defects is unenforceable

> to the extent the claims arise out of, pertain to, or relate to the negligence of the builder or the builder's other agents, other servants, or other independent contractors who are directly responsible to the builder, or for defects in design furnished by those persons, or to the extent the claims do not arise out of, pertain to, or relate to the scope of work in the written agreement between the parties.

This appears to preclude a builder from requiring indemnification from a subcontractor for the builder's sole negligence. However, CC §2782(d) permits the parties to agree that the subcontractor will defend the builder for all claims, so long as the agreement provides for reimbursement of defense fees and costs to the extent of the indemnitee's proportional liability, *i.e.,* on a comparative fault basis.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.41 d. Certificate of Insurance

§14.41 d. Certificate of Insurance

Subcontractors are often required contractually to name the project owner or the general contractor, or both, as additional insureds under their CGL policies. Compliance is confirmed by issuing policy endorsements to the additional insured parties. They often do not receive the actual endorsement, but rather are notified by way of a certificate of insurance. A certificate of insurance is merely evidence that a policy has been issued. Ins C §384. It is not a contract between the insurer and the certificate holder, and does not by itself convey additional-insured status on the holder. *Empire Fire & Marine Ins. Co. v Bell* (1997) 55 CA4th 1410, 1423, 64 CR2d 749. A certificate must state that it "does not amend, extend or alter" the coverage provided by the policy. Ins C §384(a).

A certificate of insurance issued by an authorized agent obligates the insurer to provide coverage for the certificate holder, even if the policy has not been amended to that effect. Notably, however, the certificate of insurance most commonly used in the construction industry is the Acord certificate, a single-page standardized form, which states that it "does not amend, extend or alter the coverage afforded by the referenced policies." *Diamond Woodworks, Inc. v Argonaut Ins. Co.* (2003) 109 CA4th 1020, 1032, 135 CR2d 736. Unfortunately, too often insurance brokers will issue a certificate of insurance on such a form even though they lack actual authority from the insurer to do so. In the event of a loss, the purported additional insured may have to prove that the broker had ostensible authority to issue the certificate of insurance in order for the additional insured to establish the insurer's liability. See *Preis v American Indem. Co.* (1990) 220 CA3d 752, 269 CR 617 (broker's sub-agent issued certificate without authority from insurer); *Roger H. Proulx & Co. v Crest-Liners, Inc.* (2002) 98 CA4th 182, 119 CR2d 442 (broker's employee erroneously believed issuance of certificate automatically extended coverage, but insurer required prior express approval); *American Cas. Co. v Krieger* (9th Cir 1999) 181 F3d 1113, 1122 (broker issued certificate without authority from insurer).

PRACTICE TIP: If you represent a party who is to be named as an additional insured, obtaining a Certificate of Insurance is usually sufficient. However, the "belt and suspenders" approach is to confirm your client's additional-insured status directly with the insurer.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.42 e. ISO Additional Insured Endorsements; Exclusions

§14.42 e. ISO Additional Insured Endorsements; Exclusions

Although many different forms of additional insured endorsements exist (see, *e.g.,* §14.46), the most commonly used is the ISO "20 10" endorsement. The "20 10" endorsement lists the additional insured by name (*i.e.,* as an additional named insured), and such coverage must be procured on an individual basis. Another commonly used form is the "20 30" endorsement. The "20 30" endorsement applies on a "blanket" or omnibus basis to each person or entity for whom the named insured is obligated to obtain additional insured coverage.

There are several different editions of the "20 10" endorsement, and older forms may be available through some insurers, but not others. Examples of "who is an insured" are shown in the following variations of the "20 10" endorsement:

- *CG 20 10 11 85:* WHO IS AN INSURED (Section II) is amended to include as an insured the person or persons shown in the Schedule, but only with respect to liability arising out of "your work" for that insured by or for you.
- *CG 20 10 10 93:* WHO IS AN INSURED (Section II) is amended to include as an insured the person or organization shown in the Schedule, but only with respect to liability arising out of your ongoing operations performed for that insured.
- *CG 20 10 03 97:* WHO IS AN INSURED (Section II) is amended to include as an insured the person or organization shown in the Schedule, but only with respect to liability arising out of your ongoing operations performed for that insured.
- *CG 20 10 10 01* (Beginning with this endorsement edition, bodily injury and property damage occurring after completion of work are not covered.):

  A. Section II—Who Is an Insured is amended to include as an insured the person or organization shown in the Schedule, but only with respect to liability *arising out of* **your ongoing operations** performed for that insured.
  B. With respect to the insurance afforded to these additional insureds, the following exclusion is added:
  2. Exclusions
  This insurance does not apply to "bodily injury" or "property damage" occurring after:
  1. All work, including materials, parts or equipment furnished in connection with such work on the project (other than service, maintenance or repairs) to be performed by or on behalf of the additional insured(s) at the site of the covered operations has been completed; or
  2. That portion of "your work" out of which the injury or damage arises has been put to its intended use by any person or organization other than another contractor or subcontractor engaged in performing operations for a principal as a part of the same project.

- *CG 20 10 07 04:*

  A. Section II—Who Is an Insured is amended to include as an additional insured the person(s) or organization(s) shown in the Schedule, but only with respect to liability for "bodily injury," "property damage," or "personal and advertising injury" *caused, in whole or in part, by*:
  1. Your acts or omissions; or
  2. The acts or omissions of those acting on your behalf;
  in the performance of your ongoing operations for the additional insured(s) at the location(s) designated above.
  B. With respect to the insurance afforded to these additional insureds, the following additional exclusions apply:
  This insurance does not apply to "bodily injury" or "property damage" *occurring after*:
  1. All work, including materials, parts or equipment furnished in connection with such work on the project (other than service, maintenance or repairs) to be performed by or on behalf of the additional insured(s) at the location of the covered operations has been completed; or
  2. That portion of "your work" out of which the injury or damage arises has been put to its intended use by any person or organization other than another contractor or subcontractor engaged in performing operations for a principal as a part of the same project. [Emphasis added.]

There are three key differences in the various editions of this form, discussed in §§14.43-14.45.

© The Regents of the University of California

§14.43 (1) "Arising Out of" Versus "Caused, in Whole or in Part, by"

In the pre-2004 versions of the ISO additional insured endorsement form, coverage for an additional insured was limited to liability *arising out of* the named insured's work or ongoing operations. In contrast, the 2004 version (CG 20 10 07 04) extends coverage for an additional insured to liability *caused, in whole or in part, by* acts or omissions of the named insured or those acting on behalf of the named insured.

Case law before 2004 established that the phrase "arising out of" must be given a broad meaning. *Acceptance Ins. Co. v Syufy Enters.* (1999) 69 CA4th 321, 330, 81 CR2d 557. This "minimal causal connection" is something less than proximate cause. *Vitton Constr. Co. v Pacific Ins. Co.* (2003) 110 CA4th 762, 767, 2 CR3d 1. The phrase "arising out of" has a much broader significance than "caused by." *Fibreboard Corp. v Hartford Acc. & Indem. Co.* (1993) 16 CA4th 492, 504, 20 CR2d 376. When an insurer grants coverage for liability "arising out of" the named insured's work, the additional insured is covered without regard to whether the injury was caused by the named insured or the additional insured. *Acceptance Ins. Co.,* 69 CA4th at 330; *Vitton Constr. Co.,* 110 CA4th at 768. For example, this "minimal causal connection" was held to exist when the accident occurred while the named insured was performing work for the additional insured at the worksite (*Fireman's Fund Ins. Cos. v Atlantic Richfield Co.* (2001) 94 CA4th 842, 851, 115 CR2d 26), and when the named insured cut a hole in a roof through which a worker fell, even though another subcontractor was responsible for covering the opening (*Vitton Constr. Co.,* 110 CA4th at 767).

In contrast to pre-2004 versions, the 2004 form eliminates the phrase "arising out of." The 2004 form requires that the liability be caused, in whole or in part, by acts or omissions of the named insured.

PRACTICE TIP: No cases as yet have interpreted the distinction between "arising out of" and "caused, in whole or in part, by." However, it appears that the new form will provide coverage for the additional insured's own liability, even if that liability is the major (but not sole) cause of the injury or damage, provided that the named insured's acts or omissions (or another's action on the named insured's behalf) played a part in causing the injury or damage.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.44 (2) 'Ongoing Operations'

§14.44 (2) "Ongoing Operations"

The post-1985 versions of the additional insured endorsement form limit the coverage for an additional insured to liability either arising out of or caused, in whole or in part, by the named insured's ongoing operations performed for that additional insured, depending on the form date. See §§14.42-14.43. Construction defect claims typically arise after completion of the project. This reference to "ongoing operations" eliminates coverage for "completed operations." *Pardee Constr. Co. v Insurance Co. of the W.* (2000) 77 CA4th 1340, 1359, 92 CR2d 443. On completed operations, see §§14.57, 14.67.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.45 (3) 'Acts or Omissions'

§14.45 (3) "Acts or Omissions"

The 2004 version of the additional insured endorsement form no longer refers to "your work" or "your ongoing operations." Instead, the 2004 version refers to the "acts or omissions" of the named insured or those acting on behalf of the named insured. No reported California cases have interpreted this provision. It remains to be seen whether courts will find that the change in language affects the scope of coverage afforded to the additional insured.

© The Regents of the University of California

§14.46 f. Manuscript Additional Insured Endorsements

The ISO Form CG 20 10 07 04 additional insured endorsement (see §§14.42-14.45) has not been universally adopted. Several insurers have elected to use their own additional insured endorsements, especially for insureds connected with the construction industry. These endorsements vary, and an analysis of all of them is beyond the scope of this chapter.

However, at least one major insurer uses an additional insured endorsement that provides coverage for the additional insured only if the injury or damage results from the negligence of the named insured. The 2004 ISO endorsement is not restricted on the basis of theories of liability. The only requirement in the 2004 ISO endorsement is that the named insured must have caused the injury, at least in part, by its acts or omissions. See §§14.43, 14.45. In contrast, an additional insured endorsement that restricts coverage for the additional insured to liability for the negligence of the named insured may leave the additional insured without coverage if the named insured is sued only for strict liability.

NOTE: The American Institute of Architects (AIA), Document A 201 (1997)—General Conditions of Contract for Construction, has removed entirely the requirement that the contractor name the owner as an additional insured on the contractor's liability insurance. In their 1997 commentary, the AIA observed, "while some additional protection may be gained in this way [*i.e.,* adding the owner as additional insured], it ultimately increases the cost of insurance to the contractor without measurably reducing the risk of disputes on the project." (The full AIA commentary is published on the website of the International Risk Management Institute, listed in the Directory.) The proliferation of manuscript additional insured endorsements will only increase the disputes over the rights of additional insureds.

© The Regents of the University of California

§14.47 E. Effect of Stated Policy Period on Coverage

A key inquiry under an occurrence-based policy (see §§14.12, 14.18) concerns what fact or event triggers an insurer's duty to defend or indemnify its insured. "Trigger" describes what must happen during the policy period to activate the insurer's duties to defend and indemnify. *Montrose Chem. Corp. v Admiral Ins. Co.* (1995) 10 C4th 645, 655 n2, 42 CR2d 324. The trigger of coverage usually determines which insurance policy may provide coverage. *Stonelight Tile, Inc. v California Ins. Guarantee Ass'n* (2007) 150 CA4th 19, 35, 58 CR3d 74; *Safeco Ins. Co. v Fireman's Fund Ins. Co.* (2007) 148 CA4th 620, 629, 55 CR3d 844. As defined in a standard CGL policy, an "occurrence" of "property damage" depends on when the damage took place, not when the wrongful act was committed. *Montrose Chem. Corp.,* 10 C4th at 667; *Safeco Ins. Co.,* 148 CA4th at 632. On the other hand, under the definition of "occurrence" for "personal injury" (such as wrongful eviction), it is the insured's wrongful act, not the injury to the third party claimant, that triggers coverage. *Safeco Ins. Co. v Fireman's Fund Ins. Co., supra*; *North Am. Bldg. Maintenance, Inc. v Fireman's Fund Ins. Co.* (2006) 137 CA4th 627, 633 n4, 40 CR3d 468. Put another way, the definition of "occurrence" means that property damage claims trigger policies in effect at the time of the damage; personal injury claims trigger policies in effect when the wrongful act took place. *Montrose,* 10 C4th at 669; *Safeco Ins. Co.,* 148 CA4th at 633; *North Am. Bldg. Maintenance v Fireman's Fund Ins. Co., supra*.

Under an "occurrence" policy, if an accident may have caused "bodily injury" or "property damage," at least in part, within the policy period, coverage extends to all specified harm caused by the occurrence, even if some of the harm results beyond the policy period. *Aerojet-General Corp. v Transport Indem. Co.* (1997) 17 C4th 38, 57, 70 CR2d 118. This principle of policy interpretation emphasizes the distinction between the trigger of coverage and the scope of coverage. Once coverage has been triggered, it will extend to all of the insured's liability for damages attributable to the same occurrence during and after the policy period. *FMC Corp. v Plaisted & Cos.* (1998) 61 CA4th 1132, 1184, 72 CR2d 467.

For a discussion of continuous or progressive loss, see §14.48.

© The Regents of the University of California

§14.48 1. Continuous or Progressive Loss

Under a "standard language" ISO policy, which requires that the "property damage" "occur during the policy period," if property damage is continuous and progressive through several policy periods (see §14.47), the damage is potentially covered under all policies in effect during those periods. *Montrose Chem. Corp. v Admiral Ins. Co.* (1995) 10 C4th 645, 677, 42 CR2d 324 (*Montrose II*); *Stonelight Tile, Inc. v California Ins. Guarantee Ass'n* (2007) 150 CA4th 19, 36, 58 CR3d 74; *County of San Bernardino v Pacific Indem. Co.* (1997) 56 CA4th 666, 682, 65 CR2d 657. Each insurer "on the risk when continuous or progressively deteriorating damage or injury first manifests itself remains obligated to indemnify the insured for the entirety of the ensuing damage or injury." *Montrose,* 10 C4th at 686. Each insurer has a duty separate and independent from the others to defend all the parts of the claim. *Aerojet-General Corp. v Transport Indem. Co.* (1997) 17 C4th 38, 71, 70 CR2d 118.

Successive insurers on a risk involving continuous or progressively deteriorating property damage are separately and independently obligated to indemnify the insured; each insurer is liable "in full," up to its policy limits. *Aerojet-General,* 17 C4th at 57; *Stonelight Tile, Inc. v California Ins. Guarantee Ass'n, supra*. Allocation of indemnification costs among the insurers is determined by the terms of their respective policies (*Montrose II,* 10 C4th at 681 n19):

> Allocation of the cost of indemnification once several insurers have been found liable to indemnify the insured for all or some portion of a continuing injury or progressively deteriorating property damage requires application of principles of contract law to the express terms and limitations of the various policies of insurance on the risk.

When a construction project suffers from several distinct forms of damage as a result of different construction defects, the trigger of coverage must be analyzed on a defect-by-defect basis. In other words, the fact that one defect is known will not preclude coverage for other, still latent, defects. *Chu v Canadian Indem. Co.* (1990) 224 CA3d 86, 98, 274 CR 20.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.49 2. Examples of Continuous and Progressive Damage

§14.49 2. Examples of Continuous and Progressive Damage

The following cases illustrate examples of continuous and progressive damage:

- "Extensive list of alleged design and construction defects" that caused water intrusion, mold, contamination of property, loss of use: *Standard Fire Ins. Co. v Spectrum Community Ass'n* (2006) 141 CA4th 1117, 1121, 46 CR3d 804;
- Construction defects that caused leaks, splitting and cracking of walls, floors, and ceilings, and undermining of foundation: *Pepperell v Scottsdale Ins. Co.* (1998) 62 CA4th 1045, 73 CR2d 164;
- Construction defects that caused water intrusion and dry rot: *Magnolia Square Homeowners Ass'n v Safeco Ins. Co.* (1990) 221 CA3d 1049, 271 CR 1;
- Incorporation of metallurgically substandard components that caused injury to water systems and lead contamination of water: *Watts Indus., Inc. v Zurich Am. Ins. Co.* (2004) 121 CA4th 1029, 18 CR3d 61;
- Gradual leak of water from swimming pool: *California Union Ins. Co. v Landmark Ins. Co.* (1983) 145 CA3d 462, 193 CR 461;
- Structural encroachment: *Borg v Transamerica Ins. Co.* (1996) 47 CA4th 448, 54 CR2d 811.

© The Regents of the University of California

§14.49A 3. "Known Injury or Damage" Provisions in Post-1998 ISO CGL Policies

In *Montrose Chemical Corp. v Admiral Ins. Co.* (1995) 10 C4th 645, 685, 42 CR2d 324, 913 P2d 878 *(Montrose II),* the California Supreme Court adopted the continuous trigger of coverage theory (with the result that bodily injury or property damage that is continuous or progressively deteriorating throughout successive policy periods is potentially covered by all CGL policies in effect during those periods). The Supreme Court rejected the insurer's argument that the "known loss" rule precluded coverage for continuous damage that began before the policy period. 10 C4th at 693. However, the court recognized that the continuous trigger of coverage theory did not automatically apply to policies not then under its consideration. Ultimately, coverage depends on many factors, "including the existence of express conditions or exclusions in the particular contract of insurance." 10 C4th at 655 n2.

© The Regents of the University of California

§14.49B a. ISO Policy Changes After *Montrose II*

Insurance companies are not required to use the standard ISO policy forms; they are free to modify the standard language or adopt their own nonstandard policy. See *Dart Industries, Inc. v Commercial Union Ins. Co.* (2002) 28 C4th 1059, 1074 n5, 124 CR2d 142, 52 P3d 79; *USF Ins. Co. v Clarendon America Ins. Co.* (CD Cal 2006) 452 F Supp 2d 972, 989. In response to the Montrose decision, the ISO added an endorsement to its CGL policies that took effect in most states in 1999. See *USF v Clarendon,* 452 F Supp 2d at 989. The provisions of the so-called "Known Injury or Damage" endorsement, form CG 00 57 09 99, were incorporated into the Insuring Agreement in the 2001, 2004, and 2007 ISO CGL policy forms, CG 00 01 10 01, CG 00 01 12 04, and CG 00 01 12 07.

NOTE: In the first party property insurance context, under the manifestation trigger, the insurer that insured the property at the time that appreciable property damage first becomes manifest is solely responsible for indemnification to the insured. *Prudential-LMI Commercial Ins. Co. v Superior Court* (1990) 51 C3d 674, 699, 274 CR 387, 798 P2d 1230. The "known injury or damage" policy provisions appear to incorporate this "manifestation" trigger of coverage, thus converting the occurrence form into a hybrid claims-made form.

The ISO policy revisions have given rise to decisions resulting in partial or complete denial of coverage, but have not always obviated the duty to defend. See, *e.g., Westfield Ins. Co. v Sheehan Constr. Co., Inc.* (SD Ind 2008) 580 F Supp 2d 701, 716, aff'd (7th Cir 2009) 564 F3d 817 (because insured general contractor had knowledge of defective work that allegedly damaged plaintiffs' homes prior to policy period, if "property damage" was caused by "occurrence," that damage would not be covered). In *Great American Ins. Co. of New York v North American Specialty Ins. Co.* (D Nev 2008) 542 F Supp 2d 1203, homeowners, alleging various construction defects, sued a partnership that built the homes. The court held the partnership's insurer had a duty to defend, despite conflicting evidence about whether certain damage during the policy period was a continuation, change, or resumption of property damage that existed before the policy period because, under Nevada law, any doubt about whether the duty to defend arises must be resolved in favor of the insured. See also, *IDC Construction, LLC v Admiral Ins. Co.* (SD Fla 2004) 339 F Supp 2d 1342 (interpreting similar exclusion, and holding that because complaint did not specify date when damages first occurred, insurer had duty to defend).

© The Regents of the University of California

§14.49C b. Other Anti-*Montrose II* Provisions

Although the ISO has adopted "known injury or damage" provisions to circumvent *Montrose II*'s application of the known loss doctrine, other insurers have changed the ISO CGL insuring language to require that the "bodily injury" or "property damage" be caused by an occurrence that happens during the policy period. See *USF Ins. Co. v Clarendon America Ins. Co.* (CD Cal 2006) 452 F Supp 2d 972; *Lockheed Corp. v Continental Ins. Co.* (2005) 134 CA4th 187, 35 CR3d 799, disapproved on other grounds in *State of Cal. v Allstate Ins. Co.* (2009) 45 C4th 1008, 1036 n11, 90 CR3d 1; *Westoil Terminals Co. v Industrial Indem. Co.* (2003) 110 CA4th 139, 1 CR3d 516. The *USF v Clarendon* court refused to apply the *Montrose II* "continuous injury trigger" to continuous property damage caused by construction defects, because as USF conceded, the Clarendon policies had been revised in 1996 to avoid the *Montrose II* continuous injury trigger of coverage rule (452 F Supp 2d at 989 (citations omitted)):

> The Clarendon Policies, by contrast [to *Montrose II*], require that both the occurrence and the first instance of property damage take place during the policy period. Additionally, they explicitly deem that all property damage caused contributed to by an occurrence takes place "at the time of the first such damage." This is so "even though the nature and extent of such damage or injury may change and even though the damage may be continuous, progressive, cumulative, changing or evolving, and even though the occurrence causing such bodily injury or property damage may be continuous or repeated exposure to substantially the same general harm."

The Clarendon policy provisions are explicit that progressive property damage that began before the insurers' policy period does not trigger coverage even if the damage continues into the policy period. Such property damage is outside the scope of the insuring agreement. The Clarendon Policies are not susceptible to the interpretation given to the older policy language in *Montrose II*. See *USF v Clarendon* at 989. As a result, Clarendon had no legal duty or equitable obligation to indemnify the insured. The policy provision "plainly" required the property damage to first take place during the policy period. 452 F Supp 2d at 990. Nevertheless, Clarendon did have a duty to defend the insured, with defense costs apportioned on a "time on the risk" basis. 452 F Supp 2d at 1004.

PRACTICE TIP: The foregoing cases, each involving nonstandard policy language, demonstrate the importance of carefully reviewing the language of each policy, which might apply to the loss, instead of relying on general doctrines or rules.

© The Regents of the University of California

§14.49D 4. Number of Occurrences

The definition of "occurrence" determines whether a particular policy provides coverage, but not the amount. *Safeco Ins. Co. v Fireman's Fund Ins. Co.* (2007) 148 CA4th 620, 633, 55 CR3d 844. Most CGL policies provide a larger dollar aggregate limit, and a smaller "per occurrence" dollar limit. In determining which policy limit applies, the term "occurrence" has generally been held to mean the underlying cause of the injury, rather than the injury or claim itself. When multiple injuries emanate from a common source, there is only a single "occurrence" for purposes of policy coverage. *Safeco Ins. Co. v Fireman's Fund Ins. Co., supra*. If there is only one cause, there is only one "occurrence," even if the damages extend beyond the end of the policy term. 148 CA4th at 634. Conversely, where a cause is interrupted, or when there are several autonomous causes, there are multiple "occurrences" for purposes of determining policy limits and assessing deductibles. 148 CA4th at 633.

© The Regents of the University of California

§14.50 5. After-Acquired Property

A liability insurer has no duty to indemnify or defend an insured for claims described in a third party complaint when the claims relate to property acquired by the insured after the policy period stated in the policy. *Tosco Corp. v General Ins. Co.* (2000) 85 CA4th 1016, 102 CR2d 657. This rule applies if the insured purchases new and different property after its liability policy terminated. *Tosco Corp. v General Ins. Co., supra; A.C. Label Co. v Transamerica Ins. Co.* (1996) 48 CA4th 1188, 56 CR2d 207, rejected in *K F Dairies, Inc. & Affiliates v Fireman's Ins. Fund, Inc.* (*In re K F Dairies, Inc. & Affiliates)* (9th Cir 2000) 224 F3d 922, 925. This rule also applies if the insured purchased a subsidiary company after the policy expired. *Cooper Cos., Inc. v Transcontinental Ins. Co.* (1995) 31 CA4th 1094, 37 CR2d 508.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.51 F. Liability Assumed by the Insured

§14.51 F. Liability Assumed by the Insured

The commercial general liability (CGL) policy does not normally cover indemnity obligations assumed by the insured by contract. Indemnity obligations are the reason for the special contractual liability coverage endorsement extending coverage to incidental contracts assumed by the insured. See *Shell Oil Co. v National Union Fire Ins. Co.* (1996) 44 CA4th 1633, 1642, 52 CR2d 580.

Business liability policies may extend coverage in favor of the insured by insuring contracts assumed by the insured. If a policy contains such a provision, it affords coverage not only to the insured's own conduct, but also to the acts of others for which the insured has contractually agreed to assume liability. *Old Republic Ins. Co. v Superior Court* (1998) 66 CA4th 128, 146, 77 CR2d 642, overruled on other grounds in *Vandenberg v Superior Court* (1999) 21 C4th 815, 841 n13, 88 CR2d 366. Liability "assumed under an incidental contract" that is not defined in the policy may extend coverage to any contract entered into by the insured. *Cal-Farm Ins. Co. v TAC Exterminators, Inc.* (1985) 172 CA3d 564, 578, 218 CR 407. However, nearly all policies now define the term "insured contract" or "assumed contract," and if so, the definition in the policy controls.

A contractual liability provision or coverage endorsement does not make a person an insured when that person's liability is assumed by the party insured under the policy. Rather, it extends the insurance afforded under the policy to include coverage for liability assumed by contract by the party insured. *Alex Robertson Co. v Imperial Cas. & Indem. Co.* (1992) 8 CA4th 338, 343, 10 CR2d 165. Courts should construe "insured contract" provisions broadly, in favor of coverage. *Golden Eagle Ins. Co. v Insurance Co. of the W.* (2002) 99 CA4th 837, 851, 121 CR2d 682.

The "contractual liability" provision of the 2004 CGL policy states (CG 00 01 12 04 (§I, ¶2.b), p 2):

> This insurance does not apply to:
> ….
> b. Contractual Liability
> "Bodily injury" or "property damage" for which the insured is obligated to pay damages by reason of the assumption of liability in a contract or agreement. This exclusion does not apply to liability for damages:
> (1) That the insured would have in the absence of the contract or agreement; or
> (2) Assumed in a contract or agreement that is an "insured contract", provided the "bodily injury" or "property damage" occurs subsequent to the execution of the contract or agreement. Solely for the purposes of liability assumed in an "insured contract", reasonable attorney fees and necessary litigation expenses incurred by or for a party other than an insured are deemed to be
> damages because of "bodily injury" or "property damage", provided:
> (a) Liability to such party for, or for the cost of, that party's defense has also been assumed in the same "insured contract";
> and
> (b) Such attorney fees and litigation expenses are for defense of that party against a civil or alternative dispute resolution proceeding in which damages to which this insurance applies are alleged.

"Insured contract" means (G 00 01 12 04 (§V, ¶9), p 13):

> a. A contract for a lease of premises. However, that portion of the contract for a lease of premises that indemnifies any person or organization for damage by fire to premises while rented to you or temporarily occupied by you with permission of the owner is not an "insured contract";
> b. A sidetrack agreement;
> c. Any easement or license agreement, except in connection with construction or demolition operations on or within 50 feet of a railroad;
> d. An obligation, as required by ordinance, to indemnify a municipality, except in connection with work for a municipality;
> e. An elevator maintenance agreement;
> f. That part of any other contract or agreement pertaining to your business (including an indemnification of a municipality in connection with work performed for a municipality) under which you assume the tort liability of another party to pay for "bodily injury" or "property damage" to a third person or organization. Tort liability means a liability that would be imposed by law in the absence of any contract or agreement.
> Paragraph f. does not include that part of any contract or agreement:

(1) That indemnifies a railroad for "bodily injury" or "property damage" arising out of construction or demolition operations, within 50 feet of any railroad property and affecting any railroad bridge or trestle, tracks, roadbeds, tunnel, underpass or crossing;

(2) That indemnifies an architect, engineer or surveyor for injury or damage arising out of:

(a) Preparing, approving, or failing to prepare or approve, maps, shop drawings, opinions, reports, surveys, field orders, change orders or drawings and specifications; or

(b) Giving directions or instructions, or failing to give them, if that is the primary cause of the injury or damage; or

(3) Under which the insured, if an architect, engineer or surveyor, assumes liability for an injury or damage arising out of the insured's rendering or failure to render professional services, including those listed in (2) above and supervisory, inspection, architectural or engineering activities.

The August 1996 Fire Casualty & Surety Bulletin (FC&S Bulletin), quoted in *Golden Eagle Ins. Co. v Insurance Co. of the W.* (2002) 99 CA4th 837, 847, 121 CR2d 682, clarifies that under the "current" CGL policy (now included in the 2004 CGL form), attorney fees and costs incurred by the indemnitee are included in "damages" covered under the "insured contract":

> There has been a question in some circles over whether the contractual coverage offered under the CGL form *extends defense cost coverage to the entity whose liability has been assumed by the insured through an insured contract*.... The current CGL form, in discussing liability for damages assumed under an insured contract, states that 'reasonable attorney fees and necessary litigation expenses incurred by or for a party other than an insured are deemed to be damages'. *This would seem to answer the question in the affirmative since the word 'damages' is the key word*. The exception to the contractual liability exclusion states that the exclusion does not apply to liability for 'damages' assumed under an insured contract; therefore, if the defense costs for the entity other than the insured are 'damages', the CGL form will cover them. There are some conditions to be met before the defense costs are deemed to be damages, namely, liability for the defense costs has to be assumed in the insured contract (just as the liability has to be assumed), and the defense costs have to be for defense against alleged damages that are covered by the insured's policy." (Italics added.)

© The Regents of the University of California

§14.52 G. Duty to Defend

Construction defect cases are notoriously expensive to defend. Plaintiffs often name as defendants everyone involved in the project: owners, developers, general contractors, and subcontractors. The sheer number of defendants adds to the difficulty in managing the case, not to mention the expense. Thus, establishing the client's right to a defense under one or more policies may be critical.

© The Regents of the University of California

§14.53 1. Broader Than Duty to Indemnify

The insurer's duty to indemnify runs to claims that are actually covered, in light of the facts proved. *Montrose Chem. Corp. v Admiral Ins. Co.* (1995) 10 C4th 645, 659 n9, 42 CR2d 324 (*Montrose II); Buss v Superior Court* (1997) 16 C4th 35, 45, 65 CR2d 366; *State Farm Fire & Cas. Co. v Superior Court* (2008) 164 CA4th 317, 324, 78 CR3d 828. By definition, it entails the payment of money in order to resolve liability. *Buss,* 16 C4th at 46. It arises only after liability is established. *Montrose II,* 10 C4th at 659 n9.

By contrast, the insurer's duty to defend runs to claims that are merely potentially covered, in light of facts alleged or otherwise disclosed. *Buss,* 16 C4th at 46; *Delgado v Interins. Exch. of the Auto. Club of S. Cal.* (2009) 47 C4th 302, 308, 97 CR3d 298; *Montrose Chem. Corp. v Superior Court* (1993) 6 C4th 287, 295, 24 CR2d 467 (*Montrose I)*; *Gray v Zurich Ins. Co.* (1966) 65 C2d 263, 276, 54 CR 104; *Griffin Dewatering Corp. v Northern Ins. Co. of New York* (2009) 176 CA4th 172, 97 CR3d 568; *State Farm Fire & Cas. Co. v Superior Court* (2008) 164 CA4th 317, 324, 78 CR3d 828; *Frontier Oil Corp. v RLI Ins. Co.* (2007) 153 CA4th 1436, 1464, 63 CR3d 816; *Essex Ins. Co. v City of Bakersfield* (2007) 154 CA4th 696, 704, 65 CR3d 1; *Safeco Ins. Co. v Fireman's Fund Ins. Co.* (2007) 148 CA4th 620, 629, 55 CR3d 844. It entails the rendering of a service, *i.e.,* the mounting and funding of a defense in order to avoid or at least minimize liability; it arises as soon as tender is made and is discharged when the action is concluded. *Buss,* 16 C4th at 46; *Montrose I,* 6 C4th at 295; *Frontier Oil Corp.,* 153 CA4th at 1466; *OneBeacon America Ins. Co. v Fireman's Fund Ins. Co.* (2009) 175 CA4th 183, 95 CR3d 808; *Padilla Constr. Co., Inc. v Transportation Ins. Co.* (2007) 150 CA4th 984, 996, 58 CR3d 807. It may be extinguished earlier, if it is shown that no claim can in fact be covered. *Buss,* 16 C4th at 46; *Montrose I,* 6 C4th at 295; *Frontier Oil Corp., supra*. If it is so extinguished, however, it is extinguished only prospectively and not retroactively: Before, the insurer had a duty to defend; after, it does not have a duty to defend further. *Buss,* 16 C4th at 46; *Scottsdale Ins. Co. v MV Transp.* (2005) 36 C4th 643, 655, 31 CR3d 147.

Therefore, it is frequently said that the insurer's duty to defend is broader than its duty to indemnify. *Delgado*, 47 C4th at 308 n1; *Buss,* 16 C4th at 46; *Montrose I,* 6 C4th at 295; *Scottsdale Ins. Co.,* 36 C4th 654; *Frontier Oil Corp.,* 153 CA4th at 1464. However, it is not unlimited; it extends beyond claims that are actually covered to those that are merely potentially so—but no further. *Buss,* 16 C4th at 46; *Waller v Truck Ins. Exch.* (1995) 11 C4th 1, 19, 44 CR2d 370; *State Farm Fire & Cas. Co. v Superior Court* (2008) 164 CA4th 317, 324, 78 CR3d 828.

The mere existence of a legal dispute does not create a potential for coverage. *Scottsdale Ins. Co.,* 36 C4th 643 at 657; *Griffin Dewatering Corp.,* 176 CA4th 172.

Standard language CGL policies once stated that the insurer would defend even if the allegations of the suit are groundless, false, or fraudulent. Some nonstandard language policies still contain this false claims provision. In *Gray v Zurich Ins. Co.,* the Supreme Court determined that such a false claims provision was qualified. "The 'groundless, false or fraudulent' clause however, does not extend the obligation to defend without limitation; it includes only defense to those actions of the nature and kind covered by the policy." *Gray v Zurich Ins. Co.* (1966) 65 C2d 263, 274, 54 CR 104; *Venoco, Inc. v Gulf Underwriters Ins. Co.* (2009) 175 CA4th 750, 765, 96 CR3d 409.

Some courts have held that under a contractual indemnity clause the duty to defend does not exist without a determination that the indemnitor was negligent in performing its work. *Regan Roofing Co. v Superior Court* (1994) 24 CA4th 425, 436, 29 CR2d 413. However, in *Crawford v Weather Shield Mfg., Inc.* (2008) 44 C4th 541, 565, 79 CR3d 721, the California Supreme Court disapproved the holding in *Regan Roofing Co.,* and held that the indemnitor's duty to defend arises immediately, when a claim is made against the indemnitee, regardless of any finding of fault to be made in the course of the litigation for which a defense is owed.

© The Regents of the University of California

§14.54 2. Extends to Entire Claim

Read in context, language in certain decisions stating or implying that the duty to defend is "independent" of the duty to indemnify (*Gray v Zurich Ins. Co.* (1966) 65 C2d 263, 274, 54 CR 104) means nothing more than that the former is broader than the latter. *Buss v Superior Court* (1997) 16 C4th 35, 46, 65 CR2d 366. Both the duty to indemnify and the duty to defend are in fact dependent on coverage—the former on actual coverage, the latter on at least potential coverage. *Buss,* 16 C4th at 47 n10.

Thus, in an action in which all the claims are at least potentially covered, the insurer has a duty to defend. *Buss,* 16 C4th at 47; *Hogan v Midland Nat'l Ins. Co.* (1970) 3 C3d 553, 563, 91 CR 153. See also *Horace Mann Ins. Co. v Barbara B.* (1993) 4 C4th 1076, 1081, 17 CR2d 210 (insurer has duty to defend when only one of several claims is at least potentially covered). This obligation is express in the policy's language. It rests on the fact that the insurer has been paid premiums by the insured for a defense. "The rule is grounded in basic principles of contract law." *Buss,* 16 C4th at 47.

Conversely, in an action in which none of the claims is even potentially covered, the insurer does not have a duty to defend. *Buss,* 16 C4th at 47; *Waller v Truck Ins. Exch.* (1995) 11 C4th 1, 29, 44 CR2d 370; *State Farm Fire & Cas. Co. v Superior Court* (2008) 164 CA4th 317, 324, 78 CR3d 828. This freedom is implied in the policy's language. It rests on the fact that the insurer has not been paid premiums by the insured for a defense. This "rule," too, "is grounded in basic principles of contract law." *Buss,* 16 C4th at 47.

It follows that in a "mixed" action, in which some of the claims are at least potentially covered and the others are not, the insurer has a duty to defend as to the claims that are at least potentially covered, but does not have a duty to defend as to those that are not. *Buss,* 16 C4th at 48. This conclusion is in line with the general rule that when a complaint states different causes of action against the insured, one of which is within coverage and others of which may not be, "the insurer is bound to defend *with respect to those which, if proved, would be within coverage*." *Buss,* 16 C4th at 48. "The duty to defend, although broad, is not unlimited; it is measured by the nature and kinds of risks covered." *Buss,* 16 C4th at 48; *Waller,* 11 C4th at 19.

Despite the foregoing, in a "mixed" action the insurer has a duty to defend the action in its entirety. *Buss,* 16 C4th at 48; *Horace Mann,* 4 C4th at 1081; *Padilla Constr. Co., Inc. v Transportation Ins. Co.* (2007) 150 CA4th 984, 996, 58 CR3d 807. The California Supreme Court "justified" the insurer's duty to defend the entire "mixed" action prophylactically, as an obligation imposed by law in support of the policy. *Buss,* 16 C4th at 49. To defend meaningfully, the insurer must defend immediately and entirely. *Buss,* 16 C4th at 49; *Montrose Chem. Corp. v Superior Court* (1993) 6 C4th 287, 295, 24 CR2d 467 *(Montrose I); Padilla Constr. Co., supra.* It cannot parse the claims, dividing those that are at least potentially covered from those that are not. To do so would be time consuming. It might also be futile: The "plasticity of modern pleading" (*Buss,* 16 C4th at 49; *Gray,* 65 C2d at 276) allows the transformation of claims that are at least potentially covered into claims that are not, and vice versa. The fact remains: As to the claims that are at least potentially covered, the insurer gives, and the insured gets, just what they bargained for, namely, the mounting and funding of a defense. But as to the claims that are not, the insurer may give, and the insured may get, more than they agreed, depending on whether defense of these claims necessitates any additional costs. *Buss,* 16 C4th at 49.

© The Regents of the University of California

§14.55 3. Extrinsic Evidence May Support Duty to Defend

Determination of the duty to defend depends, in the first instance, on a comparison between the allegations of the complaint and the terms of the policy. *Delgado v Interins. Exch. of the Auto. Club of S. Cal.* (2009) 47 C4th 302, 97 CR3d 298; *Montrose Chem. Corp. v Superior Court* (1993) 6 C4th 287, 295, 24 CR2d 467 *(Montrose I); Scottsdale Ins. Co. v MV Transp.* (2005) 36 C4th 643, 654, 31 CR3d 147. However, the duty also exists if extrinsic facts known to the insurer suggest that the claim may be covered. *Delgado*, 47 C4th at 308; *Montrose I,* 6 C4th at 295; *Scottsdale Ins. Co.,* 36 C4th at 654; *Frontier Oil Corp. v RLI Ins. Co.* (2007) 153 CA4th 1436, 1464, 63 CR3d 816. See also *Monticello Ins. Co. v Essex Ins. Co.* (2008) 162 CA4th 1376, 76 CR3d 848 (general contractor's insurer, as plaintiff seeking summary judgment, had burden to establish extrinsic fact that subcontractor's insurer had defect list at time when it could have decided to participate in defense).

Moreover, if, under the facts alleged, reasonably inferable, or otherwise known, the complaint could fairly be amended to allege a covered liability, the insurer still has a duty to defend even if the precise causes of action pled by the third party complaint fall outside policy coverage. *Gray v Zurich Ins. Co.* (1966) 65 C2d 263, 275, 54 CR 104; *Buss v Superior Court* (1997) 16 C4th 35, 46, 65 CR2d 366; *Scottsdale Ins. Co.,* 36 C4th at 654; *Griffin Dewatering Corp. v Northern Ins. Co. of New York* (2009) 176 CA4th 172, 97 CR3d 568; *Frontier Oil Corp.,* 153 CA4th at 1465 n21. The facts which bear on whether a claim is potentially covered include extrinsic facts known to the insurer at the inception of the suit and facts in the complaint, but do not include made-up facts, just because those facts might naturally be supposed to exist along with the known facts. *Griffin Dewatering,* 176 CA4th at 198, 97 CR3d 568; *Friedman Prof. Mgmt. Co., Inc. v Norcal Mut. Ins. Co.* (2004) 120 CA4th 17, 34-35, 15 CR3d 359; *Westoil Terminals Co., Inc. v Industrial Indemnity Co.* (2003) 110 CA4th 139, 154, 1 CR3d 516 (refusing to consider scenario not in facts of complaint); *Low v Golden Eagle Ins. Co.* (2002) 99 CA4th 109, 114, 120 CR2d 827 (refusing to consider possibility of amendment of third party's complaint against policyholder because it would speculate about unpled causes of action).

© The Regents of the University of California

§14.56 4. Reimbursement of Defense Costs

On the claims that are at least potentially covered, the insurer may not seek reimbursement for defense costs. *Buss v Superior Court* (1997) 16 C4th 35, 49, 65 CR2d 366. On the claims that are not even potentially covered, however, the insurer may indeed seek reimbursement for defense costs. 16 C4th at 50; *Scottsdale Ins. Co. v MV Transp.* (2005) 36 C4th 643, 656, 31 CR3d 147.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.57 H. Products or Completed Operations Hazard

§14.57 H. Products or Completed Operations Hazard

The standard form ISO CGL policy defines the "products or completed operations hazard" as follows (CG 00 01 12 04 (V, ¶16.a), p 14):

> a. Includes all "bodily injury" and "property damage" occurring away from premises you own or rent and arising out of "your product" or "your work" except:
> (1) Products that are still in your physical possession; or
> (2) Work that has not yet been completed or abandoned. However, "your work" will be *deemed completed* at the earliest of the following times:
> (a) When all of the work called for in your contract has been completed.
> (b) When all of the work to be done at the job site has been completed if your contract calls for work at more than one job site.
> (c) When that part of the work done at a job site has been put to its intended use by any person or organization other than another contractor or subcontractor working on the same project.
> Work that may need service, maintenance, correction, repair or replacement, but which is otherwise complete, will be treated as completed. [Emphasis added.]

The "products or completed operation hazard" clause does *not* extend the insurer's obligations beyond the policy period. (See general rules on the effect of the stated policy period in §14.47.) Thus, the "bodily injury" or "property damage" must occur after the insured has completed its "operations" on the property and during the term of the insurance policy. *Baroco W., Inc. v Scottsdale Ins. Co.* (2003) 110 CA4th 96, 103, 1 CR3d 464; *Aetna Cas. & Sur. Co. v Merritt* (9th Cir 1992) 974 F2d 1196, 1199.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.58 I. Property Damage Exclusions

§14.58 I. Property Damage Exclusions

Property damage exclusions make up a large part of CGL policies. It is beyond the scope of this chapter to discuss all the exclusions under CGL policies that might apply in a construction defect case. See, *e.g.,* California Construction Contracts, Defects, and Litigation, chaps 12, 10 (Cal CEB 2008). The exclusions discussed in §§14.59-14.68 most commonly arise in claims following real property sales transactions; some of these (see §§14.63-14.68) might apply, for example, when a property owner acts as an owner-contractor or owner-builder and before selling the property makes improvements that, after the transfer, the buyer discovers are defective.

© The Regents of the University of California

§14.59 1. Property the Insured Owns, Rents, or Occupies

The exclusion for "property damage" to real estate the insured owns, rents, or occupies occurs in the CGL policy (CG 00 01 12 04 (§I, ¶2.j(1)), p 4), in the Businessowners Coverage Form (BP 00 03 07 02 (§II.B, ¶1.k(1)), p 31), and in the Owners and Contractors Protective Liability policy (CG 00 09 12 04 (§I, ¶1.g(1)), p 3).

In *Old Republic Ins. Co. v Superior Court* (1998) 66 CA4th 128, 150, 77 CR2d 642, overruled on other grounds in *Vandenberg v Superior Court* (1999) 21 C4th 815, 841 n13, 88 CR2d 366, the court considered a virtually identical exclusion, which provided that the insurance would not apply to property damage to "property owned or occupied by or rented to the insured." 66 CA4th at 138. The insureds had leased commercial property for 10 years. The lessor then sued them for breach of the lease agreement and waste, alleging the insureds breached the lease by (66 CA4th at 135)

> failing and refusing to keep and maintain the leased premises… in good order, condition and repair and, upon the surrender of the leased premises…, to return them to the lessor in the same condition as when received, ordinary wear and tear excepted, clean and free of debris with all damages repaired….

Specifically, the lessor alleged that the insureds (66 CA4th at 136 n5)

> caused extensive damage to the Property including, but not limited to, damage to the ceilings, floors, fixtures and carpets, caused by, among other things, deterioration of the roof and the failure and/or refusal to maintain the premises….

The insureds carried liability insurance with different insurers during the leasehold period. All denied coverage and all refused a defense except for one, which later sued the other three insurers for contribution, equitable indemnity, and declaratory relief. The insurers unsuccessfully moved for summary judgment, but the appellate court granted their petition for writ of mandate. In addition, the court held that, even assuming the underlying action was covered under the policies' insuring clause, there would still be no coverage because of the "owned, occupied or rented" exclusion in each of the insurers' policies. The court held that (66 CA4th at 150)

> [o]n its face, this exclusion unambiguously precludes coverage for any claim for property damage to property occupied or rented to the [insureds]. Since that is precisely what the underlying action was about, this exclusion would preclude coverage in any event.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.60 2. Alienated Premises

§14.60 2. Alienated Premises

The "alienated premises" exclusion precludes coverage for property damage to premises the insured sells, gives away, or abandons. It occurs in the CGL policy (CG 00 01 12 04 (§I, ¶2.j(2)), p 4) and the Businessowners Coverage Form (BP 00 03 07 02 (§II.B, ¶1.k(2)), p 31). There is no comparable exclusion in the Owners and Contractors Protective Liability policy (CG 00 09 12 04).

The Alienated Premises exclusion is stated as follows:

> "Property damage" to:
> ….
> (2) Premises you sell, give away or abandon, if the "property damage" arises out of any part of those premises.

Other variations of the exclusion state that there is no coverage for "property damage to premises alienated by the named insured arising out of such premises or any part thereof." *Maryland Cas. Co. v Reeder* (1990) 221 CA3d 961, 976, 270 CR 719. On exclusions for injury or damage arising out of the sale, see §14.85.

In *Maryland Cas. Co. v Reeder, supra,* the court held that the "alienated premises" exclusion did not apply to an insured who had owned the premises before the policy took effect. Pearlman had owned the land, but conveyed it to a partnership in which he was a partner. The partnership formed a joint venture with a corporation, and the joint venture retained a contractor to build condominiums. Ownership of the premises was transferred to the joint venture. At various times, Pearlman, the partnership, the joint venture, and the contractor were named insureds under a series of CGL policies. Despite Pearlman's interest in the condo as a partner and joint venturer, the court held the alienated premises exclusions did not apply to Pearlman's liability, because he did not own the premises at any time during the policy period. 221 CA3d at 978. However, the alienated premises exclusion did preclude coverage for the joint venture; although the joint venture would be covered for claims for injury or damage during construction, the exclusion barred coverage for any claims against the joint venture arising after conveyance of the property. 221 CA3d at 978.

The August 1982 Fire Casualty & Surety Bulletin warns that when, in addition to the comprehensive general liability coverage, an insured has purchased a broad form endorsement (221 CA3d at 976 (quoting Bulletin):

> "It is important to alert insureds—particularly those who buy land, build on it, and then sell the improved property—that the Broad Form Property Damage endorsement has no effect on the so-called Alienated Premises exclusion common to Premises and Operations and Completed Operations Liability insurance. That exclusion eliminates coverage for property damage to premises alienated (*e.g.,* sold) by the named insured, if the damage arises out of such premises or any part thereof. Say, for example, that the named insured buys a lot and then, acting as general contractor, builds a house on the lot. If, after the house is completed and sold, a subcontractor's faulty wiring causes the house to burn and the buyer sues the named insured for the costs of repairing the house, the named insured will have no coverage under Broad Form Property Damage (including Completed Operations) endorsement, due to the Alienated Premises exclusion. By the same token, if the same named insured had not been the owner of the property but only the general contractor, he would presumably have had coverage under his Broad Form endorsement for all property damage to the house other than, perhaps, the faulty work of the subcontractor or the 'particular part' of the subcontractors' work in which the fire originated."

This exclusion does not apply, however, if the insured is not an owner when the work was completed, or if the damage was caused by a subcontractor who was not an insured. 221 CA3d at 977.

Another reported case interpreting the alienated premises exclusion summarized it this way: Although the exclusion is intended to "deny coverage to an insured who has failed to repair property prior to its sale or who has failed to disclose the existence of a defect in the premises at the time of sale," it was not intended to prevent coverage "to the completed operations of a contractor" who has constructed residential units for resale. Nevertheless, the exclusion has been used "in conjunction with other 1973 CGL policy provisions to preclude coverage for construction-related property damage claims that probably should have fallen within the coverage intent of the policy." See *Prudential-LMI Commercial Ins. Co. v Reliance Ins. Co.* (1994) 22 CA4th 1508, 1512, 27 CR2d 841, quoting Wielinski & Gibson, Broad

Form Property Damage Coverage, p 99 (3d ed 1992).

© The Regents of the University of California

§14.61 3. Property Loaned to Insured

This exclusion, which eliminates coverage for property damage to property loaned to the insured, occurs in the CGL policy (CG 00 01 12 04 (§I, ¶2.j(3), p 4), the Businessowners Coverage Form (BP 00 03 07 02 (§II.B, ¶1.k(3)), p 31), and the Owners and Contractors Protective Liability policy (CG 00 09 12 04 (§I, ¶1.g(2)), p 3).

There are apparently no reported decisions interpreting this exclusion. In regard to real property, it is difficult to conceive of a scenario in which it could be "loaned." In regard to personal property, it would appear that this exclusion seldom applies. If personal property is valuable enough to support a lawsuit, it seems unlikely that it would be "loaned" without some contractual indemnity provision. If valuable personal property were loaned, it would likely also fall within the exclusion for personal property in the "care, custody or control" of the insured (see §14.62), thus avoiding any dispute over the meaning of the term "loaned."

© The Regents of the University of California

§14.62 4. Property Damage to Personal Property in Care, Custody, or Control of the Insured

This exclusion, which eliminates coverage for property damage to personal property in the care, custody, or control of the insured, occurs in the CGL policy (CG 00 01 12 04 (§II.B, ¶1.j(4)), p 4), the Businessowners Coverage Form (BP 00 03 07 02 (§II.B, ¶1.k(4)), p 31), and the Owners and Contractors Protective Liability policy (CG 00 09 12 04 (§I, ¶1.g(3)), p 3). Each of these exclusions is currently expressly limited to personal property. Other versions of this exclusion in other policies may extend the exclusion to real property.

For example, in *Allstate Ins. Co. v Chaney* (ND Cal 1992) 804 F Supp 1219, Matson bought a house from the Chaneys. Later, Matson sued the Chaneys, alleging that they intentionally or negligently misrepresented the condition of the property and concealed numerous defects, including a structurally unsound garage, plumbing defects, defective sewer lines that were not connected to the municipal sewer, drainage problems, and electrical wiring problems. 804 F Supp at 1220 n3. The Chaneys' homeowners policy contained an exclusion that excluded coverage for "property damage to property rented to, occupied by or in the care of an insured…." 804 F Supp at 1223. The court noted the undisputed fact that the Chaneys owned the property until the close of escrow on May 21, 1991. The property was "occupied, used by or in the care of" the Chaneys until they vacated the property on May 24, 1990—the day before Matson took possession. Because at least some of the "property damage" alleged by Matson necessarily had to have occurred before the date Matson came into possession of the premises, the court held that the policy excluded coverage for such damage. 804 F Supp at 1223.

In *Volf v Ocean Acc. & Guar. Corp.* (1958) 50 C2d 373, 325 P2d 987, Volf, a general contractor, constructed a house for Hoover. A stucco exterior finish applied by Volf cracked. Hoover filed a claim with the State Contracting Board, and the board ordered Volf to apply a new stucco exterior. Volf then sued his CGL carrier for the cost of the repair. Exclusion "g" in the CGL policy excluded coverage for injury to or destruction of "(3)… property in the care, custody or control of the insured." 50 C2d at 374. The appellate court held that the damage was excluded under Exclusion "g" of the policy. 50 C2d at 375. Since the defective cement was used and the cracks appeared in the stucco while Volf was constructing the house and before Hoover took possession, the loss was occasioned by "injury to… property in the care, custody or control of the insured" and was therefore excluded under Exclusion "g". 50 C2d at 375.

In *Employers Ins. of Wausau v California Water Serv. Co.* (ND Cal, Aug. 25, 2008, No. C-06-03002 RMW) 2008 US Dist Lexis 65433, the California Department of Toxic Substance Control (DTSC) filed lawsuits against the insured, alleging that the insured and others contaminated a groundwater aquifer. The insurer began an action to resolve a coverage dispute. The policy excluded coverage for damage to "any property" (not just personal property) in the "care, custody or control of the insured held for sale or storage." The insurer argued that this exclusion barred coverage because the insured is a purveyor of water, and water from the contaminated aquifer would eventually pass through the insured's system to be sold to consumers; thus, any property damage must be to water "in the care, custody or control" of the insured. The district court held the argument to be "without merit," noting that the DTSC brought the actions for damages for contamination of the aquifer, not of the water in the insured's system.

© The Regents of the University of California

§14.63 5. Work Performed

A significant exclusion relating to construction defect claims eliminates coverage for property damage to that particular part of real property on which the insured, or any contractor or subcontractor working directly or indirectly on behalf of the insured, is performing operations, if the "property damage" arises out of those operations; it is called the "Work Performed" Exclusion. This provision occurs in the CGL policy (CG 00 01 12 04 (§II.B, ¶1.j(5)), p 5) and the Businessowners Coverage Form (BP 00 03 07 02 (§II.B, ¶1.k(5)), p 31). The provision in the Owners and Contractors Protective Liability policy (CG 00 09 12 04 (§I, ¶1.g(4)), p 3) excludes coverage for "'Property damage' to 'work' performed for you by the 'contractor.'"

This exclusion, and CGL exclusion (j)(6) (see §14.64), reflect the purpose of liability insurance policies for contractors:

> The risk intended to be insured is the possibility that the… work of the insured, once relinquished or completed, will cause bodily injury or damage to property other than to the product or completed work itself. [Citation.]… [T]he effect of the policy is to make the contractor stand its own replacement and repair losses while the insurer takes the risk of injury to the property of others.

Western Employers Ins. Co. v Arciero & Sons, Inc. (1983) 146 CA3d 1027, 1031, 194 CR 688; see also *CalFarm Ins. Co. v Krusiewicz* (2005) 131 CA4th 273, 31 CR3d 619*; Maryland Cas. Co. v Imperial Contracting Co.* (1989) 212 CA3d 712, 723, 260 CR 797.

The exclusion represents the principle that the risk of replacing or repairing the insured's defective work or product is a commercial risk that is not passed on to the liability insurer. *CalFarm Ins. Co.,* 131 CA4th at 287; *F & H Constr. v ITT Hartford Ins. Co.* (2004) 118 CA4th 364, 373, 12 CR3d 896 (liability insurance policy not designed to serve as performance bond or warranty of contractor's product); *Maryland Cas. Co. v Reeder* (1990) 221 CA3d 961, 967, 270 CR 719 (liability policies not designed to provide contractors and developers with coverage against claims that their work is inferior or defective). Thus, the exclusion "precludes coverage for liability for damage to and deficiencies of the insured contractor's work product," and it "applies to the insured's defective work as well as to the insured's satisfactory work that is damaged by the insured's defective work." *Diamond Heights Homeowners Ass'n v National Am. Ins. Co.* (1991) 227 CA3d 563, 571, 277 CR 906; *CalFarm Ins. Co.,* 131 CA4th at 287.

The August 1982 Fire Casualty & Surety Bulletin (FC & S Bulletin), published by the National Underwriters Association, explains that the usual Completed Operations coverage (with no Broad Form Property Damage endorsement attached) flatly excludes property damage to work performed by or on behalf of the named insured arising out of the work. Under the usual coverage, then, the insured has no insurance whatsoever for damage to a subcontractor's work, or for damage to the insured's own work resulting from a subcontractor's work.

However, under an endorsement affording Broad Form Property Damage coverage including Completed Operations, the phrase "on behalf of" the named insured is eliminated. Thus, the "work performed" exclusion in the broad form endorsement

> eliminates coverage for property damage to work performed by the named insured if the property damage arises out of the named insured's work or any portion of it. Thus, an insured has coverage for his completed work when the damage arises out of work performed by someone other than the named insured, such as a subcontractor….

Maryland Cas. Co. v Reeder (1990) 221 CA3d 961, 972, 270 CR 719 (quoting FC & S Bulletin); *Insurance Co. of N. Am. v National Am. Ins. Co.* (1995) 37 CA4th 195, 201, 43 CR2d 518; *Roger H. Proulx & Co. v Crest-Liners, Inc.* (2002) 98 CA4th 182, 202, 119 CR2d 442.

© The Regents of the University of California

6. Faulty Workmanship

§14.64 a. No Coverage for Defective Building Parts Caused by Work Incorrectly Performed

Another significant exclusion relating to construction defect claims eliminates coverage for property damage to that particular part of any property that must be restored, repaired, or replaced because the "work" of the insured (as defined) was incorrectly performed on it. This exclusion occurs in the CGL policy (CG 00 01 12 04 (§II.B, ¶1.j(6)), p 5) and the Businessowners policy (BP 00 03 07 02 (§II.B, ¶1.k(6)), p 31). The exclusion in the Owners and Contractors Protective Liability policy (CG 00 09 12 04 (§I, ¶1.g(4)), p 3) excludes coverage for "'Property damage' to 'work' performed for you by the 'contractor.'"

This is generally referred to as the "faulty workmanship" exclusion. This exclusion does not preclude coverage for faulty workmanship that is covered by virtue of the products-completed operations hazard clause (see §14.57).

Third party owners' complaints generally fall into two classifications: (1) alleged defective materials and (2) faulty workmanship. *St. Paul Fire & Marine Ins. Co. v Coss* (1978) 80 CA3d 888, 892, 145 CR 836. With regard to faulty workmanship, an insurer of a contractor does not undertake to insure the "cost of repair" or damage to roofs, heaters, hot water heaters, flooring, or windows if there is no property damage to the building structure itself. *Rafeiro v American Employers' Ins. Co.* (1970) 5 CA3d 799, 809, 85 CR 701 (third party judgment did not set forth the existence of any property damage).

© The Regents of the University of California

§14.65 b. Damage to Building Caused by Removal of Defective Materials and Faulty Workmanship Distinguished

Under the faulty workmanship exclusion, installation of defective materials into a building (*e.g.,* stucco that cracked before and after completion of the structure) is excluded. *Volf v Ocean Acc. & Guar. Corp.* (1958) 50 C2d 373, 325 P2d 987. Similarly, installation of defective doors is excluded, but damage to other property (*i.e.,* other parts of the structure) caused by removal of defective doors in order to replace them, is covered. *Geddes & Smith, Inc. v St. Paul Mercury Indem. Co.* (1959) 51 C2d 558, 564, 334 P2d 881; see also *Maryland Cas. Co. v Reeder* (1990) 221 CA3d 961, 971, 270 CR 719; *Rafeiro v American Employers' Ins. Co.* (1970) 5 CA3d 799, 807, 85 CR 701.

In the case of a general contractor, all the work at the project is considered its work product. In the case of a subcontractor, only the subcontractor's portion of the work is the work product. Damage to other parts of the project is considered damage to other property. *George F. Hillenbrand, Inc. v Insurance Co. of N. Am.* (2002) 104 CA4th 784, 805, 128 CR2d 586.

The faulty workmanship exclusion eliminates coverage for the cost of repair to "other property" incidental to repairing the defective workmanship. *Golden Eagle Ins. Co. v Travelers Cos.* (9th Cir 1996) 103 F3d 750, 757. The court in *Hillenbrand* opined that *Golden Eagle* does not address the pertinent issue of whether damage to "other property" caused by a subcontractor's work is covered. *George F. Hillenbrand, Inc.,* 104 CA4th at 805.

© The Regents of the University of California

§14.66 7. Product Exclusion: Damage to Your Product

The exclusion in the 2004 CGL policy (CG 00 01 12 04 (§I, ¶2.k), p 5) and the Businessowners policy (BP 00 03 07 02 (§II.B, ¶1.*l*), p 31) excludes coverage for:

> "Property damage" to "your product" arising out of it or any part of it and included in the "products-completed operations hazard".

See §14.57. Both policies define "your product" as follows (CG 00 01 12 04 (§V, ¶21), p 15; BP 00 03 07 02 (§II.F, ¶21), p 40):

> "Your product":
> a. Means:
> (1) Any goods or products, other than real property, manufactured, sold, handled, distributed or disposed of by:
> (a) You;
> (b) Others trading under your name; or
> (c) A person or organization whose business or assets you have acquired; and
> (2) Containers (other than vehicles), materials, parts or equipment furnished in connection with such goods or products.
> b. Includes
> (1) Warranties or representations made at any time with respect to the fitness, quality, durability, performance or use of "your product"; and
> (2) The providing of or failure to provide warnings or instructions.
> c. Does not include vending machines or other property rented to or located for the use of others but not sold.

In *Watts Indus., Inc. v Zurich Am. Ins. Co.* (2004) 121 CA4th 1029, 18 CR3d 61, the insured manufactured and sold parts for municipal water systems. These parts contained greater amounts of lead or zinc, and lower amounts of copper, than contract specifications required. 121 CA4th at 1035. The insured was sued for selling substandard parts; the companies knowingly defrauded the municipalities and violated the False Claims Act. Govt C §12651(a)(1)-(2), (8). In particular, the plaintiff alleged that the substandard parts wore out sooner than parts required by the contract; that the municipalities and their water customers had been harmed by increased lead exposure from the substandard parts, which contained 40 percent more lead; and that the substandard parts would have to be dug up and replaced at more than 70,000 sites. 121 CA4th at 1036. Notably, on appeal, the insured conceded that damage to the substandard parts themselves was excluded from the CGL coverage by the "your product" exclusion. 121 CA4th at 1046.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.67 8. Work Completed Exclusion: Damage to Your Work

§14.67 8. Work Completed Exclusion: Damage to Your Work

The "damage to your work" exclusions in the CGL (CG 00 01 12 04 (§1, ¶2.*l*), p 5) and the Businessowners policy (BP 00 03 07 02 (§II.B, ¶1.m), p 31) exclude coverage for:

> "Property damage" to "your work" arising out of it or any part of it and included in the "products-completed operations hazard". [See §14.57.]
> This exclusion does not apply if the damaged work or the work out of which the damage arises was performed on your behalf by a subcontractor.

Both policies define "your work" as follows (CG 00 01 12 04 (§V, ¶22), p 15; BP 00 03 07 02 (§II.F, ¶22), p 40):

> "Your work":
> a. Means:
> (1) Work or operations performed by you or on your behalf; and
> (2) Materials, parts or equipment furnished in connection with such work or operations.
> b. Includes
> (1) Warranties or representations made at any time with respect to the fitness, quality, durability, performance or use of "your work", and
> (2) The providing of or failure to provide warnings or instructions.

The CGL policy defines "products-completed operations hazard" as follows (CG 00 01 12 04 (§V, ¶16), p 14):

> "Products-completed operations hazard":
>
> a. Includes all "bodily injury" and "property damage" occurring away from premises you own or rent and arising out of "your product" or "your work" except:
> (1) Products that are still in your physical possession; or
> (2) Work that has not yet been completed or abandoned. However, "your work" will be deemed completed at the earliest of the following times:
> (a) When all of the work called for in your contract has been completed.
> (b) When all of the work to be done at the job site has been completed if your contract calls for work at more than one job site.
> (c) When that part of the work done at a job site has been put to its intended use by any person or organization other than another contractor or subcontractor working on the same project.
> Work that may need service, maintenance, correction, repair or replacement, but which is otherwise complete, will be treated as completed.
> b. Does not include "bodily injury" or "property damage" arising out of:
> (1) The transportation of property, unless the injury or damage arises out of a condition in or on a vehicle not owned or operated by you, and that condition was created by the "loading or unloading" of that vehicle by any insured;
> (2) The existence of tools, uninstalled equipment or abandoned or unused materials; or
> (3) Products or operations for which the classification, listed in the Declarations or in a policy schedule, states that products-completed operations are subject to the General Aggregate Limit.

See also BP 00 03 07 02 (§II.F, ¶16), p 39, which has a similar definition.

In *Collett v Insurance Co. of the W.* (1998) 64 CA4th 338, 75 CR2d 165, Collett, a masonry contractor, built a series of retaining walls for Dividend Development in connection with a residential development. The retaining walls failed, and Collett agreed to remove and rebuild them, up to a cost of $125,000, as a settlement of claims against him by Dividend Development. Collett claimed that its CGL insurer, Insurance Company of the West (ICW), had agreed to indemnify him for these costs under the property damage provisions of his commercial general liability policy. When ICW refused to do so, Collett sued for breach of contract and breach of the covenant of good faith and fair dealing. 64 CA4th at 339. The exclusion was summarized in the opinion as follows (64 CA4th at 341):

> Under exclusion L [exclusion in CG 00 01 12 04, §1, ¶2.*l*] (the work completed exclusion), the CGL policy did not cover: "'Property damage' to 'your work' arising out of it or any part of it and included in the 'products-completed operations hazard.'" The products-completed operations hazard includes all property damage arising out of "your product" or "your work" except work that has not yet been completed. Exclusion

L did not apply (*i.e.,* the property damage was covered) "if the damaged work or the work out of which the damage arises was performed on your behalf by a subcontractor."

Collett argued the exclusion for "your work" did not apply because the inspector Collett hired to inspect the retaining walls and make sure they were being built according to specifications negligently failed to do so. Collett argued that the inspector was a "subcontractor" and thus the inspector's negligence fell within the exception to the exclusion. The appellate court disagreed, holding that the exclusion barred coverage for the claim. 64 CA4th at 344. The court noted that, even under a broad interpretation of the term "subcontractor," the inspector was not a subcontractor: "While the inspector may have failed to catch defects in the retaining walls, he did not put them there. Collett did." 64 CA4th at 343.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.68 9. Damage to 'Impaired Property' {§14.72}

§14.68 9. Damage to "Impaired Property" {§14.72}

The "damage to impaired property" exclusion in the CGL policy (CG 00 01 12 04 (§1, ¶2.m), p 5) and Businessowners policy (BP 00 03 07 02 (§II.B, ¶1.n), p 32) excludes coverage for:

> "Property damage" to "impaired property"… arising out of:
> (1) A defect, deficiency, inadequacy or dangerous condition in "your product" or "your work."
> ….

"Impaired property" is defined as (CG 00 01 12 04 (§V, ¶8), p 12; BP 00 03 07 02 (§II.F, ¶8), p 37):

> [T]angible property, other than "your product" or "your work", that cannot be used or is less useful because:
> a. it incorporates "your product" or "your work" that is known or thought to be defective, deficient, inadequate or dangerous;
> ….
> if such property can be restored to use by:
> a. The repair, replacement, adjustment or removal of "your product" or "your work";
> ….

This exclusion reflects the principle that the risk of replacing or repairing a defective product is considered a commercial risk that is not passed on to a liability insurer. *Shade Foods, Inc. v Innovative Prods. Sales & Mktg., Inc.* (2000) 78 CA4th 847, 866, 93 CR2d 364. The impaired property exclusion does not apply when the other property (which incorporates the allegedly faulty work or product) has been physically injured. For example, when the complaint alleges explicitly that the mere replacement of a part will not fully restore the damaged property, the exclusion will not apply. *Watts Indus., Inc. v Zurich Am. Ins. Co.* (2004) 121 CA4th 1029, 1047, 18 CR3d 61.

© The Regents of the University of California

§14.68A J. The "Pollution Exclusion"

Before 1966, the standard form CGL policy did not contain any specific exclusion for pollution. Many courts construed the policy to cover damages resulting from long-term, gradual exposure to environmental pollution. See *MacKinnon v Truck Ins. Exch.* (2003) 31 C4th 635, 643, 3 CR3d 228. Beginning in 1970, the standard form CGL policy added the "qualified pollution exclusion." This exclusion permitted coverage of "sudden and accidental" pollution. 31 C4th at 643. Litigants disputed the meaning of the terms "sudden" and "abrupt" and many courts held that gradual pollution was not excluded. 31 C4th at 644.

In 1985, the standard form CGL policy replaced the "qualified pollution exclusion" with what is now referred to as the "absolute pollution exclusion," which (1) eliminated any requirement that the discharge be "sudden and accidental," and (2) eliminated the requirement that pollution be discharged "into or upon land, the atmosphere or any watercourse or body of water." *MacKinnon,* 31 C4th at 644. Even the "absolute pollution exclusion" is limited to "traditional environmental pollution." *MacKinnon,* 31 C4th at 653. Examples of "traditional environmental pollution" (not covered) include:

- Dirt and rocks discharged by quarry operator into creek (*Ortega Rock Quarry v Golden Eagle Ins. Corp.* (2006) 141 CA4th 969, 990, 46 CR 3d 517);
- Widespread dissemination of silica dust as an incidental by-product of the insured's sandblasting operations (*Garamendi v Golden Eagle Ins. Co.* (2005) 127 CA4th 480, 486, 25 CR3d 642); and
- Persistent, widespread dissemination of offensive odors and dust from insured's normal operation of its composting facility (*Cold Creek Compost, Inc. v State Farm Fire & Cas. Co.* (2007) 156 CA4th 1469, 1480, 68 CR3d 216).

Examples of releases held *not* to constitute "traditional environmental pollution" (and which were thus covered) include:

- Negligent use of pesticides by spraying to eradicate yellow jackets around an apartment building (*MacKinnon v Truck Ins. Exch.* (2003) 31 C4th 635, 654, 3 CR3d 228); and
- Accidental, one-time release of high concentration of ammonia into air surrounding insured's plant, and not part of insured's normal operations (*SEMX Corp. v Federal Ins. Co.* (SD Cal 2005) 398 F Supp 2d 1103, 1118).

Some insurers now offer a "pollution buy back provision." The court in *Venoco, Inc. v Gulf Underwriters Ins. Co.* (2009) 175 CA4th 750, 757, 96 CR3d 409 held that such a pollution exclusion will not apply if the insured establishes that (1) the event is an unintended and unexpected accident; (2) the accident can be identified as commencing at a specific time and date; (3) the accident is not the result of an intentional violation of a government statute, rule, or regulation; and (4) the occurrence became known to the insured within 7 days after its commencement and was reported to the insurer within 60 days thereafter. Under this provision, compliance with the reporting requirement is enforceable without proof of prejudice. 175 CA4th at 760.

Some insurers have now adopted the total pollution exclusion endorsement, which supposedly is more favorable to the insurer. See *Griffin Dewatering Corp. v Northern Ins. Co. of New York* (2009) 176 CA4th 172, 178 n3, 97 CR3d 568 ("To the degree that there may be any difference between the 'total pollution exclusion' and the more common 'absolute pollution exclusion,' it appears that the 'total' one excludes a little more than the 'absolute' one, that is, less favorable to the insured.")

© The Regents of the University of California

K. Personal and Advertising Injury

§14.69 1. Insuring Language

"Bodily injury" and "property damage" are defined in terms of the injury or damage that results from any type of "accidental" conduct. In contrast, "personal injury" is defined not in terms of the injury or harm that results, but in terms of the conduct that produces it. Personal injury coverage applies to injury that arises out of the commission of certain enumerated acts or offenses. Coverage is triggered by the offense, not the injury or damage that a plaintiff suffers. *Fibreboard Corp. v Hartford Acc. & Indem. Co.* (1993) 16 CA4th 492, 511, 20 CR2d 376. While these offenses should be construed broadly to encompass all specific torts that could reasonably fall within the general category (16 CA4th at 515), the scope of personal injury liability coverage under standard form CGL policies cannot be expanded beyond the offenses enumerated above (*American Guar. & Liab. Ins. Co. v Vista Med. Supply* (ND Cal 1988) 699 F Supp 787, 793 (applying California law)). See also *Golden Eagle Ins. Corp. v Cen-Fed, Ltd.* (2007) 148 CA4th 976, 990, 56 CR3d 279 (definition of "personal injury," which included wrongful eviction or wrongful entry into or invasion of the right of private occupancy of room, dwelling, or premises occupied by "person," referred to "natural person" and did not extend to interference with property leased by corporation).

Like "personal injury," "advertising injury" is a term of art used in many liability policies, and, like "personal injury," is typically defined to mean injury arising from certain enumerated "offenses" in the course of advertising activities. Beginning with the 1996 CGL form, "advertising injury" means injury arising out of one or more of the following offenses:

- Slander, libel, or disparagement of another's goods, products, or services;
- Violation of right of privacy;
- "Misappropriation of advertising ideas or style of doing business"; or
- "Infringement of copyright, title or slogan."

See ISO Form CG 00 01 01 96 (§V, ¶1). This provision eliminates the offenses of "unfair competition" and "piracy" found in earlier forms, but adds the offense of "misappropriation of advertising ideas or style of doing business."

The 1998 and later CGL forms combine "advertising injury" and "personal injury" offenses into "personal and advertising injury," defined as (CG 00 01 12 04(§V, ¶14), p 14):

> injury, including consequential "bodily injury" arising out of one or more of the following offenses:
> a. False arrest, detention or imprisonment;
> b. Malicious prosecution;
> c. Wrongful eviction from, wrongful entry into, or invasion of the right of private occupancy of a room, dwelling or premises that a person occupies, committed by or on behalf of its owner, landlord or lessor;
> d. Oral or written publication, in any manner, of material that slanders or libels a person or organization or disparages a person's or organization's goods, products or services;
> e. Oral or written publication, in any manner, of material that violates a person's right of privacy;
> f. Use of another's advertising idea in your "advertisement"; or
> g. Infringing upon another's copyright, trade dress or slogan in your "advertisement".

On the defined term "occurrence" and when it is "triggered" in cases of property damage or personal injury, see §14.47.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.70 2. Exclusions

§14.70 2. Exclusions

The personal and advertising injury liability coverage contains its own exclusions. Some of these exclusions are for "personal and advertising injury"

- for which the insured has assumed liability in a contract or agreement;
- arising from a breach of contract;
- arising from the failure of goods, products, or services to conform to statements of quality or performance;
- arising from the wrong description of the price of goods, products, and services; or
- arising from the infringement of copyright, patent, trademark, trade secret, or other intellectual property rights.

See CG 00 01 12 04 (§1, Coverage B, §2), p 6.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.71 IV. SPECIAL ISSUES: BUSINESSOWNERS LIABILITY

§14.71 IV. SPECIAL ISSUES: BUSINESSOWNERS LIABILITY

The ISO Businessowners policy (BOP) (BP 00 06), is another commonly used form, but it is an earlier edition and was merged into form BP 00 03 07 02. See §14.4. See also the ISO summary, which is available on the website listed in the Directory. The liability insuring language, exclusions, and definitions of the BOP policy are, for the most part, substantively the same as the comparable provisions of the CGL policy. For that reason, the issues that arise under the BOP policy in regard to a real estate transaction will be substantially similar to those under a CGL policy. Those issues are:

- *"Occurrence"; "Accident"*. The use and definition of the term "occurrence" in the BOP policy is the same as that in the CGL policy. See §§14.18-14.24.
- *Property Damage*. The insuring language and definition of "property damage" in the BOP policy is the same as that in the CGL policy. See §§14.25-14.27.
- *Bodily Injury*. The insuring language and definition of "bodily injury" in the BOP policy is the same as that in the CGL policy. See §§14.28-14.30.
- *Who Is an Insured*. The section in the BOP policy regarding "Who Is An Insured" is substantially similar to the same section in the CGL policy. See §§14.31-14.45.
- *Contractual Liability; Liability Assumed by the Insured; Insured Contracts*. The principles that govern coverage for liability assumed by the insured or under an "insured contract" under the BOP policy are the same as those under the CGL policy. See §14.51.
- *Personal and Advertising Injury Liability*. The insuring language and exclusions regarding personal and advertising injury coverage are nearly the same in the BOP policy as in the CGL policy. See §§14.69-14.70.
- *Duty to Defend*. The principles regarding the duty to defend under the BOP policy are the same as those under the CGL policy. See §§14.52-14.56.
- *Products or Completed Operations*. The policy language and definition of "products or completed operations" under the BOP policy are the same as those under the CGL policy. See §14.57.
- *Exclusions*. Most of the exclusions in the BOP policy are identical to those in the CGL policy (see §§14.58-14.68), except for the Professional Services Exclusion.
- *Professional Services Exclusion*. The BOP policy contains an exclusion that is not in the CGL policy. Instead of a definition of "professional services," the exclusion sets forth a nonexclusive list of professional services. It precludes liability for (CG 00 03 07 02 (§II.B, ¶1.j), p 31):

> "Bodily injury", "property damage", "personal and advertising injury" caused by the rendering or failure to render any professional service. This includes but is not limited to:
> (1) Legal, accounting or advertising services;
> (2) Preparing, approving, or failing to prepare or approve maps, drawings, opinions, reports, surveys, change orders, designs or specifications;
> (3) Supervisory, inspection or engineering services;
> (4) Medical, surgical, dental, x-ray or nursing services treatment, advice or instruction;
> (5) Any health or therapeutic service treatment, advice or instruction;
> (6) Any service, treatment, advice or instruction for the purpose of appearance or skin enhancement, hair removal or replacement or personal grooming;
> (7) Optometry or optical or hearing aid services including the prescribing, preparation, fitting, demonstration or distribution of ophthalmic lenses and similar products or hearing aid devices;
> (8) Body piercing services; and
> (9) Services in the practice of pharmacy.

In *Hollingsworth v Commercial Union Ins. Co.* (1989) 208 CA3d 800, 256 CR 357, Hollingsworth was insured as the sole proprietor of a cosmetics store. Her merchants insurance policy excluded coverage for "bodily injury or property damage due to the providing of, or failure to provide, any professional service." At the time Hollingsworth purchased the policy, her store sold earrings, but did not pierce customers' ears. During the policy term, the store began providing ear

piercing, for a fee. A customer sued after she was injured when a store employee pierced her ears. The insurer denied coverage, based on the "professional services" exclusion.

Hollingsworth relied on dictionary definitions of the term "professional" as "a calling requiring specialized knowledge and often long and intensive academic preparation." 208 CA3d at 806. She argued that since ear piercing is not regulated by the state, does not require licensing, and consists simply of mechanically operating the ear-piercing tool, it did not qualify as a "professional service." 208 CA3d at 806. The appellate court disagreed. First, the court noted that dictionary definitions of "professional" also included "a broad range of activities beyond those traditionally considered 'professions,' such as medicine, law or engineering" and included "participating for gain or livelihood in an activity or field of endeavor often engaged in by amateurs." 208 CA3d at 806. The court concluded that "the term 'professional services' is not as narrowly circumscribed as Hollingsworth proposes. Rather, it generally signifies an activity done for remuneration as distinguished from a mere pastime." 208 CA3d at 807. Second, the court considered the exclusion in the context of the policy as a whole. 208 CA3d at 807. The court explained that "in determining whether a particular act is of a professional nature or a 'professional service' we must look not to the title or character of the party performing the act, but to the act itself," and cited out-of-state authority holding that a liability policy issued to a beauty parlor clearly was meant to include as "professional services" the technical work performed by the beauticians. 208 CA3d at 807. The court held (208 CA3d at 808):

> [I]n the context of a cosmetics business, ear piercing clearly constitutes a professional service as distinguished from an activity incidentally related to its everyday operations. Such an enterprise is devoted to grooming and the improvement of personal appearance for which jewelry can be a significant enhancement. And, although Hollingsworth did not charge a monetary fee for piercing a customer's ears, neither was it performed gratis. The procedure was offered only with the purchase of a pair of earrings. Undoubtedly, attracting prospective purchasers into the store also provided additional economic incentive to Hollingsworth. Thus, the ear-piercing was a "professional" service both in the sense that it constituted an aspect of the cosmetics sales profession and that it was done for and in anticipation of some form of financial gain.

See also *Tradewinds Escrow, Inc. v Truck Ins. Exch.* (2002) 97 CA4th 704, 118 CR2d 561 (professional-services exclusion excluded all potential coverage and insurer had no duty to defend claims of misrepresentation, constructive trust, accounting, conversion, unfair business practices, and intentional infliction of emotional distress against insured escrow company arising out of failed sale of home, because alleged wrongful acts were committed during performance of professional services, namely, rendering of escrow services); *Stone v Hartford Cas. Co.* (CD Cal 2006) 470 F Supp 2d 1088 (professional services exclusion precluded coverage for liability based on insured's professional undertaking to draft plans for room additions, construct and/or supervise construction of the additions, and install a driveway).

NOTE: The exclusion in the ISO BOP policy specifically includes "[p]reparing, approving, or failing to prepare or approve maps, drawings, opinions, reports, surveys, change orders, designs or specifications," along with "supervisory, inspection or engineering services." This appears to eliminate liability coverage under a BOP policy for many potential claims against contractors, architects, engineers, and surveyors. Moreover, even if "professional services" were not excluded, an insured would face an uphill battle obtaining coverage for such claims. BOP and CGL policies limit coverage to "accidental" occurrences, and generally do not provide coverage for professional negligence claims. *Ray v Valley Forge Ins. Co.* (1999) 77 CA4th 1039, 1047, 92 CR2d 473; for examples of conduct held to not be "accidental," see §14.21. Furthermore, coverage for "bodily injury" and "property damage" does not include economic damages resulting from negligence. *Allstate Ins. Co. v Interbank Fin. Servs.* (1989) 215 CA3d 825, 830, 264 CR 25. On property damage, see §14.25; on bodily injury, see §14.28.

In *Food Pro Int'l v Farmers Ins. Exchange* (2008) 169 CA4th 976, 89 CR3d 1, the court held that the insured's services as an engineering consultant for equipment installation, including high-level supervision of the overall plant relocation, were "professional services" within the meaning of a professional services exclusion. 169 CA4th at 987. However, the court further held that a tort action against the insured by a construction worker injured during the relocation when the worker was injured as a result of performing a project ordered by the foreman rather than by the insured, was potentially outside the scope of the exclusion. and consequently, the insurer had a duty to defend.

NOTE: The *Food Pro* case demonstrates that though an insured may generally provide "professional services," the focus should be on the specific acts giving rise to liability.

© The Regents of the University of California

§14.72 V. SPECIAL ISSUES: REAL ESTATE AGENTS' ERRORS AND OMISSIONS LIABILITY POLICY

Professional liability policies are written for real estate licensees, both agents and brokers. See §14.8. The liability policies provide for defense of the insured as well as indemnity. *Morris v Employers Reinsurance Corp.* (2000) 84 CA4th 1026, 1029, 101 CR2d 350.

© The Regents of the University of California

§14.73 A. Claims Made

Like other errors and omissions policies, coverage for real estate agents and brokers is almost always written on a "claims made" basis. On "claims made" policies, see §14.13; see also §14.15 on extended reporting period.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.74 B. Representative Insuring Clause

§14.74 B. Representative Insuring Clause

The following is a representative insuring clause in a real estate agents' and brokers' liability policy:

> The Company will pay on behalf of the Insured all sums which the Insured shall become legally obligated to pay as Damages for Claims first made against the Insured during the Policy Period and first reported to the Company in writing during the Policy Period or within sixty (60) days thereafter, arising out of any act, error, omission or Personal Injury in the rendering of or failure to render Professional Services by an Insured covered under this policy; provided always that such act, error, omission or Personal Injury happens:
>
> A. During the Policy Period; or
>
> B. Prior to the Policy Period provided that:
>
> 1. Such act, error, omission or Personal Injury happened on or after the Prior Acts Date as indicated on the Declarations Page of this policy; and
>
> 2. At the inception of this policy the Insured had no reasonable basis to believe that any Insured had breached a professional duty and no reasonable basis to believe an act, error or omission might be expected to result in a Claim or Suit.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.75 C. Exclusions

§14.75 C. Exclusions

A typical real estate agents' and brokers' errors and omissions liability policy excludes coverage for loss arising out of or related to the following:

> Dishonest, fraudulent, criminal, or malicious acts or omissions, or intentional misrepresentations;
> Arising out of any disputes involving any Insured's fees, commissions or charges
> Made by an Insured against any other Insured, unless such Claim arises solely out of Professional Services performed for that party in a broker-client capacity;
> Based on or arising out of the rendering of or failure to render Professional Services by any Insured as employee, owner, partner, stockholder, director or officer of any sole proprietorship, partnership, Limited Liability Partnership/Corporation, corporation or other business enterprise not listed on the Declarations Page.
> Arising out of:
> Bodily Injury, sickness, disease or death of any person; or
> Physical injury, damage to or destruction of or loss of use of tangible property;
> However, this exclusion does not apply to the performance of Professional Services by an Insured in the maintenance, operation or use of a lock box on property not owned, occupied by or leased to an Insured.
> Based on or arising out of activities involving property syndication, real estate investment trusts, limited partnerships or similar investments;
> Based on or arising out of the sale or purchase of insurance, or the failure to effect or maintain adequate levels or types of insurance;
> Based on or arising out of liability assumed by an Insured under any oral or written contract or agreement, including any warranty, except that this exclusion shall not apply to liability the Insured would have in the absence of such contract, agreement or warranty;
> Arising out of activities of an Insured as a mortgage banker, mortgage counselor, mortgage broker, business broker, independent third party escrow agent, contractor, construction advisor, property developer, insurance agent or insurance broker;
> Involving real property owned by any Insured.
> This exclusion shall not apply if:
> Title is held by an Insured for less than one year for the purpose of resale, or
> The property is a single-family dwelling owned by an Insured and listed for sale by another Insured who owns no part of it.
> Resulting from:
> Injury, disease or illness (including death at any time resulting therefrom);
> Damage to or reduction in financial value of any property; or
> Other loss or expense arising in whole or in part, out of or in any way related to Asbestos;
> Arising out of any guarantee or promise of future status, performance or valuation in the course of performing Professional Services by the Insured;
> Based on or arising out of the Insured gaining, in fact, any personal profit or advantage to which any Insured is not legally entitled, including misappropriation, conversion, embezzlement, commingling or defalcation of funds or other property.
> Arising out of, based on, alleging or arising out of discrimination of any kind by an Insured, including but not limited to discrimination due to or on the basis of age, sex, race, color, religion, disability, marital status, pregnancy, national origin, HIV or AIDS status, sexual origin, sexual orientation, or sexual preference.

Because professional liability insurance for real estate agents and brokers is designed to cover risks in selling property for others, such policies commonly exclude claims involving property owned by the insured or an entity in which the insured has a financial interest, *i.e.,* situations in which the broker or agent deals with his or her own inventory. See *Morris v Employers Reinsurance Corp.* (2000) 84 CA4th 1026, 101 CR2d 350. In *Morris,* the exclusion stated (84 CA4th at 1028):

> This policy does not apply to:… (e) any claim made against the Insured arising out of or in connection with any property, entity or enterprise controlled, managed, operated, or in which there is an ownership interest by: (1) An insured; (2) A member of an insured's immediate family….

This exclusion by its terms would not apply to an agent or broker who attempts to acquire an equitable interest in

property from a seller, thereby acting in conflict of interest with the agent/broker's client who made an offer on the property in question. The exclusion does not apply for the simple reason that when the agent/broker attempts to purchase the property, "her very act of attempting to purchase the property from [seller] reveals that she [agent/broker] was not dealing with her own property…." 84 CA4th at 1030. Accordingly, this conduct places the insured's conduct outside the purview of exclusion (e).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.76 VI. SPECIAL ISSUES: REPRESENTATIONS AND WARRANTIES INSURANCE

§14.76 VI. SPECIAL ISSUES: REPRESENTATIONS AND WARRANTIES INSURANCE

Representations and warranties (R&W) liability insurance has historically been used primarily in connection with corporate mergers and acquisitions, often regarding compliance with applicable tax rules, intellectual property matters, product liability issues, accounting and financial issues, employment practices, and environmental matters. However, several companies now offer R&W insurance in connection with real estate transactions outside the mergers and acquisitions context. See §14.9. Possible uses include insurance coverage for breach of representations and warranties as to:

- Acquisitions of real estate by asset purchase, merger, or purchase of entity interests;
- Allocation provisions in partnership or operating agreements for historic or low income tax credits; or
- The validity of certain permits for use or operations.

There is no standard-language ISO R&W policy. Typically, however, an R&W policy will identify the party to be indemnified (the buyer) as the "Insured." The indemnitor is typically identified as "Seller." "Reps & Warranties" or "R&W" is defined as those representations and warranties of the Seller in favor of the Insured and contained in a specifically identified contract or agreement. The contract or agreement containing the subject representations and warranties is identified as the "R&W Contract." "R&W Loss" is defined as "a loss incurred by Insured which arises out of breach of the Reps & Warranties."

Thus, the R&W insurance is not limited to "property damage" or "bodily injury" or "personal and advertising injury" as are CGL and BOP policies. R&W insurance extends to the resulting financial losses if specifically identified representations and warranties are untrue.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.77 A. Representative Insuring Language

§14.77 A. Representative Insuring Language

As mentioned above, there is no standardized insuring language. The insuring language typically reads:

> pursuant to this Insuring Clause, and subject to the terms, conditions, deductibles, retentions, exclusions, and Aggregate Policy Limit hereinafter set forth, Insurer will indemnify Insured for R&W Losses sustained directly by Insured to the extent Seller is liable to Insured for R&W Losses under [Section __] of the R&W Contract.

© The Regents of the University of California

§14.78 B. Claims Made

Nearly all companies that offer R&W Insurance write it on a "claims made" basis. See §14.13.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.79 C. Exclusions

§14.79 C. Exclusions

There is no standardized form Representations and Warranties policy, so there are no "standard" exclusions. However, many policies will contain exclusions for the following:

- Tax liability;
- Closing or balance sheet adjustments;
- Breaches of which the insured had actual knowledge at closing;
- Projections;
- Liability assumed by the insured under the subject representations and warranties contract, or any loss of which the insured had actual knowledge as of the closing of the transaction; and
- Failure of the insured to fulfill a condition precedent set forth in the transactional documents.

© The Regents of the University of California

VII. SPECIAL ISSUES: HOMEOWNERS LIABILITY

§14.80 A. Insuring Language

There are several commonly used versions of the ISO Homeowners policy: the Homeowners 3 Special Form (HO 00 03); the Broad Form (HO 00 02); and the Unit Owners Form (HO 00 06), which is used for condominiums. These forms differ principally in the property coverage each provides in Section I (see chap 13). Section II, which provides liability coverage, is virtually identical in each form. Like CGL and BOP policies, most homeowners policies provide coverage for "bodily injury" and "property damage" caused by an "occurrence." However, they do not provide "advertising injury" or "personal injury" coverage, as these are usually associated with commercial risks. The policies are similar to the CGL policies with respect to the following features:

- "Occurrence"; "Accident"; see §§14.18-14.24.
- Property Damage; see §§14.25-14.27.
- Bodily Injury; see §§14.28-14.30.
- Duty to Defend; see §§14.52-14.56.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.81 B. Exclusions

§14.81 B. Exclusions

Although there are several other exclusions in the homeowners policy, the ones most likely to arise in a real estate transaction are discussed in §§14.82-14.85.

© The Regents of the University of California

§14.82 1. Business

"Bodily injury" or "property damage" arising out of or in connection with a "business" conducted from an "insured location" or engaged in by an "insured" are excluded from a typical homeowners policy.

"Business" is usually defined in a homeowners policy form as follows:

> a. A trade, profession or occupation engaged in on a full-time, part-time or occasional basis; or
> b. Any other activity engaged in for money or other compensation, except the following:
> (1) One or more activities, not described in (2) through (4) below, for which no "insured" receives more than $2,000 in total compensation for the 12 months before the beginning of the policy period;
> (2) Volunteer activities for which no money is received other than payment for expenses incurred to perform the activity;
> (3) Providing home day care services for which no compensation is received, other than the mutual exchange of such services; or
> (4) The rendering of home day care services to a relative of an "insured".

Perhaps because homeowners policies are not intended to insure business or commercial activities, courts interpreting the "business pursuits" exclusion have given a broad interpretation to the term "business." For example, in *Fire Ins. Exch. v Jiminez* (1986) 184 CA3d 437, 229 CR 83, the appellate court cited prior decisions that held that the principal factor in whether some activity is a "business" is the motivation to make money (184 CA4th at 442):

> [A]pplicability of the business pursuit exclusion turns on the motivation for the pursuit[,]… the presence of the profit motive carries considerable weight, and that the business engaged in need not be the sole occupation. Part-time business activities are also included under business pursuits exclusions. [Citation.] [¶] Other jurisdictions have defined a business pursuit as a regular activity engaged in for the purpose of earning a profit. This includes part-time or supplemental income projects.

The court therefore held that an insured's demolition of a lean-to shed, which was considered a nuisance on his commercial property, was a "business" activity because it would enhance the value of the property. 184 CA4th at 442. Further, the court rejected the insured's argument that the demolition was a "one-time decision" not a "regular activity" and thus not a "business" because the argument too narrowly focused on the decision to tear down the shed, rather than the fact that the insured had been engaged in the business of owning the property for profit for several years. 184 CA4th at 443.

However, if an activity has both business and nonbusiness purposes, the "nonbusiness pursuit" exception to the business-pursuits exclusion allows coverage. *Crane v State Farm Fire & Cas. Co.* (1971) 5 C3d 112, 95 CR 513 (nonbusiness-pursuit exception applies when insured provided child care services to others while taking care of own children).

© The Regents of the University of California

§14.83 2. Professional Services

Coverage for "bodily injury" or "property damage" arising out of the rendering of or failure to render professional services (see, *e.g.,* policies described in §§14.6-14.7) is excluded from a typical homeowners policy.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/14 Liability Insurance: Selected Issues Pertinent to Sales/§14.84 3. Noninsured Location

§14.84 3. Noninsured Location

Coverage for "Bodily injury" or "property damage" arising out of a premises owned, rented to, or rented by an insured that is not an insured location are excluded from a typical homeowners policy.

© The Regents of the University of California

§14.85 4. Arising Out of the Sale

Although the ISO Homeowners policy does not contain one, some homeowners policies contain a specific exclusion for bodily injury or property damage:

> arising out of the sale or transfer of real property, including but not limited to the following:
> (a) known or unknown property or structural defects;
> (b) known or hidden defects in the plumbing, heating and electrical systems;
> (c) known or unknown soil conditions or drainage problems;
> (d) concealment or misrepresentation of any known defects.

See, *e.g., Davis v Farmers Ins. Group* (2005) 134 CA4th 100, 106, 35 CR3d 738.

This type of "sale or transfer" exclusion has been held to exclude coverage following a transfer for bodily injuries (such as sinus and respiratory infections) allegedly caused by mold or fungi. 134 CA4th at 103, 106. See also discussion of the alienated premises exclusion in §14.60.

© The Regents of the University of California

15

Escrow and Closing the Sale

Peter Brian Bothel
Laura S. Lowe

I. WHAT IS AN ESCROW?
- A. Definition §15.1
  - 1. Who Can Be an Escrow Holder? §15.2
  - 2. Who Regulates Escrow? §15.3
    - a. Independent Escrow Companies §15.4
    - b. Internet Escrow Agents §15.5
    - c. Parties Exempt From Escrow Law §15.6
- B. How Is an Escrow Created? §15.7
- C. Northern California Versus Southern California Distinctions §15.8

II. PARTIES TO ESCROW §15.9
- A. Escrow Officers §15.10
- B. Buyers and Sellers §15.11
- C. Attorneys §15.12
- D. Lenders §15.13
- E. Brokers §15.14
- F. Title Insurer §15.15

III. FUNCTIONS OF ESCROW HOLDER
- A. Generally §15.16
- B. Residential Transactions §15.17

IV. ESCROW HOLDER'S DUTIES
- A. Limited Agency §15.18
- B. Fiduciary Responsibilities §15.19
- C. Disclosures to Parties §15.20
- D. Duty to Disclose Fraud §15.21

V. LIABILITY OF ESCROW HOLDER
- A. Liability to Parties to Escrow §15.22
- B. Liability to Nonparties §15.23
- C. Accommodation Recordings §15.24
- D. Escheat §15.25

VI. DEPOSIT INTO ESCROW AND ITS CONSEQUENCES
- A. Conditional Delivery §15.26
- B. Effect on Title and Possession
  - 1. Before Conditions Are Satisfied §15.27
  - 2. After Conditions Are Satisfied §15.28
  - 3. Waiver of Conditions §15.29

VII. THIRD PARTY DEMANDS §15.30

VIII. ESCROW INSTRUCTIONS
- A. General Provisions §15.31
- B. California Association of Realtors® Contract §15.32
- C. Preparation of Escrow Instructions §15.33
  - 1. Property Description §15.34
  - 2. Deposit of Funds
    - a. Good Funds Law §15.35
    - b. Right of Escrow Holder to Commingle Funds §15.36

c. Interest on Deposits §15.37
3. Drafting Documents §15.38
4. Leases §15.39
5. Title Insurance §15.40
6. Executing and Delivering Documents §15.41
7. Closing; Closing Costs §15.42
8. Prorations §15.43
a. Real Property Taxes and Assessments §15.44
b. Insurance Premiums §15.45
c. Rent §15.46
9. Recordation; Priority §15.47

IX. SUPPLEMENTAL ESCROW INSTRUCTIONS TO PURCHASE AGREEMENT AND JOINT ESCROW INSTRUCTIONS §15.48
A. Buyer's Supplemental Escrow Instructions §15.49
1. Form: Introduction §15.50
2. Form: Deposits by Buyer §15.51
3. Form: Conditions Precedent to Close of Escrow §15.52
4. Form: Title Insurance Requirements §15.53
5. Form: Estimated Closing Statement §15.54
6. Form: Procedure for Closing §15.55
7. Form: Time for Closing Escrow; Investment of Funds §15.56
8. Form: Prorations §15.57
9. Form: Authorized Disbursements; Costs §15.58
10. Form: Right to Withdraw Documents or Funds §15.59
11. Form: Document Approval §15.60
12. Form: Acknowledgment by Escrow Holder §15.61
B. Seller's Supplemental Escrow Instructions §15.62
1. Form: Introduction §15.63
2. Form: Deposits by Seller §15.64
3. Form: Conditions Precedent to Close of Escrow §15.65
4. Form: Procedure for Closing §15.66
5. Form: Time for Closing Escrow §15.67
6. Form: Prorations; Costs §15.68
7. Form: Authorized Disbursements; Costs §15.69
8. Form: Payment of Broker's Commission §15.70
9. Form: Right to Withdraw Documents or Funds §15.71
10. Form: Document Approval §15.72
11. Form: Acknowledgment by Escrow Holder §15.73
C. Lender's Instructions §15.74

X. TAX ISSUES
A. California Withholding
1. Withholding Requirements §15.75
2. Individual Exemptions to Withholding Requirements §15.76
3. Nonindividual Exemptions to Withholding Requirements §15.77
4. No Waiver for Individuals §15.78
5. Buyer's Obligations; Penalties §15.79
B. FIRPTA
1. Withholding Requirements §15.80
2. Exemptions to Withholding Requirements §15.81
3. Form: Certification of Nonforeign Status by Corporation, Partnership, Trust or Estate §15.82
4. Withholding Certificate §15.83
5. Buyer's Obligations; Penalties §15.84

XI. CLOSING THE DEAL
A. Why Record? §15.85
B. Effect of Recording §15.86
C. Defects or Exceptions to Constructive Notice §15.87
D. Procedures for Recording
1. Form of Instrument §15.88
2. Acknowledgments §15.89
3. Place of Recording §15.90
4. Recorder's Procedure §15.91
5. Timing of Recording §15.92

E. Processing Documents; Disbursing Funds §15.93
F. Real Estate Commission §15.94
G. Real Estate Settlement Procedures Act (RESPA) §15.95
H. Holdbacks §15.96

XII. FAILED TRANSACTIONS
A. Cancellation of Escrow §15.97
B. Interpleader §15.98

XIII. PRELIMINARY CHANGE OF OWNERSHIP REPORT §15.99

© The Regents of the University of California

I. WHAT IS AN ESCROW?

§15.1 A. Definition

An escrow is defined as a "legal document or property delivered by a promisor to a third party to be held by the third party for a given amount of time or until the occurrence of a condition, at which time the third party is to hand over the document or property to the promisee." Black's Law Dictionary (8th ed 2004).

Escrow is statutorily defined as follows (Fin C §17003(a)):

> "Escrow" means any transaction in which one person, for the purpose of effecting the sale, transfer, encumbering, or leasing of real or personal property to another person, delivers any written instrument, money, evidence of title to real or personal property, or other thing of value to a third person to be held by that third person until the happening of a specified event or the performance of a prescribed condition, when it is then to be delivered by that third person to a grantee, grantor, promisee, promisor, obligee, obligor, bailee, bailor, or any agent or employee of any of the latter.

In the real estate context the escrow holder is the third party who receives the deed (conveying title to the buyer), deed of trust (conveying a security interest to the lender), and the funds. The escrow releases the documents and funds when all of the conditions to closing the escrow, as set forth in the escrow instructions, occur. Generally, the deed may be recorded when the escrow holder has received adequate funds to pay for the real property. The deed of trust may be recorded when the funds are in escrow awaiting distribution to the seller and the buyer takes title. The deed of trust is generally recorded concurrently with the deed. The proceeds are released to the seller when the deed and deed of trust are recorded.

© The Regents of the University of California

§15.2 1. Who Can Be an Escrow Holder?

An escrow agent is defined as "any person engaged in the business of receiving escrows for deposit or delivery." Fin C §17004. In the real estate context, the types of companies that engage in the escrow business differ between Northern California and Southern California. See §15.8. In Northern California, escrow holders are generally sister companies or subsidiaries of title insurance companies. In Southern California, many escrows are handled by independent escrow companies that are unaffiliated with title insurance companies.

Attorneys and real estate brokers may also act as escrow holders, subject to certain limitations. See §15.6. Attorneys should be careful not to inadvertently become an escrow holder, thus acquiring a fiduciary duty to a nonclient. If the attorney accepts a document for delivery on the fulfillment of a condition from a client or a nonclient, the attorney may incur liability to either for any damage for failure to follow instructions. *Wasmann v Seidenberg* (1988) 202 CA3d 752, 248 CR 744. In California real estate transactions, attorneys generally delegate the duties of escrow holder to a separate escrow company.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.3 2. Who Regulates Escrow?

§15.3 2. Who Regulates Escrow?

Escrow companies are regulated by two different departments, depending on who owns the escrow company. Independent escrow companies are regulated by the Department of Corporations. Fin C §§17000-17703; see §15.4. Escrow companies that are controlled or owned by a title insurance company (sister company or subsidiary) are regulated by the Department of Insurance and are exempt from the Escrow Law (Fin C §§17000-17703). Ins C §12340.6; see §15.6.

© The Regents of the University of California

§15.4 a. Independent Escrow Companies

Independent escrow companies are corporations licensed and regulated by the state Department of Corporations under the Escrow Law (Fin C §§17000-17703). The Commissioner of Corporations has adopted numerous regulations covering the activities of independent escrow companies. See 10 Cal Code Regs §§1700-1769. The Escrow Law requires these escrow companies to do the following:

- Maintain records (Fin C §17404);
- Submit an audit report to the commissioner (Fin C §17406);
- Keep escrow funds (includes escrows described in Fin C §17312(c) and other escrows) in a separate trust account (Fin C §17409);
- Transfer funds between escrow accounts by written instruments or, in the case of Internet escrow companies (see §15.5), by wire transfer, evidence of which may be maintained in electronic form (Fin C §17409.1); and
- Obtain fidelity bonds on officers and employees who have access to funds (Fin C §17203.1).

A violation of any of these requirements can result in a fine of up to $10,000, imprisonment in a state prison or up to a year in county jail, or both a fine and imprisonment. Fin C §17700. In addition, a civil penalty not to exceed $2500 may be recovered from a licensed escrow company that violates any statutory requirement or rule. Fin C §17701.

The Escrow Agents' Fidelity Corporation (EAFC), a nonprofit corporation established under the Escrow Law, acts as the fidelity surety for the trust obligations of licensed escrow agents in California. Fin C §§17300-17350. A claim against an independent escrow company is made against the EAFC, which in turn pursues the alleged wrongdoer. See, *e.g., Escrow Agents' Fid. Corp. v Superior Court* (1992) 4 CA4th 491, 5 CR2d 698.

Required membership in the EAFC is now limited to licensees who engage, in whole or in part, in the business of receiving escrows for deposit or delivery in the following types of transactions (Fin C §17312(c)):

- Real property escrows, including the sale, lease, exchange, or transfer of title, and loans or other obligations to be secured by a lien on real property;
- Bulk sale escrows, including the sale, lease, exchange, or transfer of title to a business entity and the transfer of liquor licenses or other types of business licenses or permits;
- Fund or joint control escrows;
- The sale, transfer of title, or refinance escrows for manufactured homes or mobilehomes;
- Reservation deposits held in escrow accounts as required under the public report section of the Subdivided Lands Act (Bus & P C §§11000-11200) or by regulation of the Department of Real Estate; and
- Escrows for sale, transfer, modification, assignment, or hypothecation of promissory notes secured by deeds of trust.

The Commissioner of Corporations may enforce the Escrow Law by ordering discontinuance of business operations (Fin C §17415), revoking or suspending the escrow company's license (Fin C §17608), taking possession of the property and business of an escrow company (Fin C §17621), bringing an action to enjoin acts or practices or to enforce compliance (Fin C §17607), or seeking a liquidation of the business (Fin C §17635).

© The Regents of the University of California

§15.5 b. Internet Escrow Agents

An "Internet escrow agent" means anyone engaged in the business of receiving escrows for deposit or delivery over the Internet. Fin C §17004.5. An Internet escrow agent is included within the definition of "escrow agent." Fin C §17005.6. All escrow records may be retained by an Internet escrow agent and provided to the Commissioner in electronic format. Fin C §17403.5.

© The Regents of the University of California

§15.6 c. Parties Exempt From Escrow Law

Banks, savings and loan associations, insurance companies, title companies, real estate brokers, and attorneys may also act as escrow holders without being licensed or regulated as independent escrow companies because they are exempt from California's Escrow Law. Fin C §17006. The exemption for attorneys applies only to attorneys not actively engaged in the business of an escrow agent, while real estate brokers can act as escrow agents only in the course of, or incidental to, a real estate transaction. Fin C §17006(a). This exemption is "not available for any arrangement entered into for the purpose of performing escrows for more than one business." Fin C §17006(b). See §2.22. This exemption scheme was upheld in *Escrow Inst. v Pierno* (1972) 24 CA3d 361, 100 CR 880. No other persons or entities can handle escrows for compensation. Fin C §17200.

© The Regents of the University of California

§15.7 B. How Is an Escrow Created?

An escrow is created when a party gives the escrow holder documents or funds to be held pending the satisfaction of a condition. It is customary for the buyer to choose the escrow holder to be used in the transaction. Generally escrow is opened when the buyer deposits instructions and funds to be held pending satisfaction of the conditions described in the instructions.

Escrow instructions are generally written. If the parties are using the California Association of Realtors® (CAR) residential purchase agreement and joint escrow instructions form (CAR Contract) (see §§6.24, 15.32), the escrow holder usually signs the form contract accepting the escrow and signaling the opening of the escrow. In Northern California, some of the local boards of realtors use a real estate contract that is unique to the particular county (*e.g.,* San Francisco and Marin counties). These unique contracts do not contain escrow instructions. In those counties where the CAR Contract is not in use, the escrow holder commonly receives the deposit of funds with oral instructions—rather than written instructions—to, in essence, hold the funds for the purpose of closing an escrow regarding certain property. Oral instructions are valid and instructions need not be in writing. See *Kirk Corp. v First Am. Title Co.* (1990) 220 CA3d 785, 270 CR 24; *Zang v Northwestern Title Co*. (1982) 135 CA3d 159, 185 CR 176.

© The Regents of the University of California

§15.8 C. Northern California Versus Southern California Distinctions

Northern and Southern California handle escrows differently. As discussed in §15.15, independent escrow companies are common in Southern California, while in Northern California escrow companies are often related to or controlled by title insurance companies.

Historically, the other major distinction between Northern and Southern California is that in Southern California the parties sign escrow instructions at the beginning of the transaction (using amendments to meet the changing conditions of the transaction), while in Northern California escrow instructions are often signed and deposited in escrow only a few days before closing. This practice has created much frustration for everyone because problems are often discovered only when escrow instructions are signed. It is easier to resolve problems without delaying close of escrow if the problems are discovered earlier in the transaction.

This historic difference is mollified—at least for residential transactions—by use of the California Association of Realtors® (CAR) residential purchase agreement and joint escrow instructions form (see §§6.24, 15.32). This contract includes escrow instructions with the purchase agreement; thus, the escrow instructions are signed at the beginning of the transaction. Under the terms of the CAR form, the contract is given to the escrow holder within 3 days of acceptance by the seller. If the CAR contract is used as intended, escrow practice in Northern and Southern California should become more similar.

For further discussion of the differences in escrow procedures between Northern and Southern California, see California Title Insurance Practice §§3.29-3.30, 10.3 (2d ed Cal CEB 1997).

© The Regents of the University of California

§15.9 II. PARTIES TO ESCROW

Many parties may be involved in an escrow, and each has a distinct role. It is crucial that attorneys understand the roles that the parties play in order to understand the positions that the escrow holder must take in a transaction, and the limitations on the escrow holder's role.

Various individuals and companies interact with the escrow holder. Some are parties to the escrow, while others are not. Whether an individual or company is a party or a nonparty is crucial to the ability of that individual or company to give escrow instructions. The buyer, seller, escrow holder, and buyer's lender are all parties to the escrow. Depending on the broker's contract, the broker may be a limited party to the escrow. See §§15.14, 15.94. The seller's lender and other lien holders are not parties to the escrow without an assignment of proceeds from a party to the escrow. See §15.30. Although the attorney representing a seller, buyer, or lender will definitely interact with the escrow holder, the attorney is not a party to the escrow. See §15.12.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.10 A. Escrow Officers

§15.10 A. Escrow Officers

The escrow officer is the independent, neutral third party who is hired to follow the parties' escrow instructions. Escrow officers are usually trained in-house, starting as escrow assistants and handling the more mundane aspects of the transaction. Escrow assistants order payoff demands, draw simple instructions, fill out many of the forms, and monitor the status of the transaction. Escrow officers typically meet with the clients, prepare the escrow instructions, draw the checks, fill out the necessary financial information, and arrange for recording the necessary documents. Many escrow officers specialize in certain types of transactions.

PRACTICE TIP: Counsel for the parties should make certain that the escrow officer is well suited for the transaction. For instance, most companies have a national commercial services unit that works on multistate, large, complex commercial transactions. Some of the national commercial services' escrow officers specialize further by working on closing large franchise transactions. Other escrow officers may specialize in refinancing transactions, mobilehome transactions, or ranch lands and vineyards. Each type of transaction has its unique issues, and a specialist will be knowledgeable about those pertaining to his or her area of expertise.

© The Regents of the University of California

§15.11 B. Buyers and Sellers

The buyer and the seller are the key figures in a real estate escrow transaction. Only the buyer and the seller may instruct the escrow holder, absent a court order. The buyer and the seller may instruct the escrow holder to allow others to become a party to the escrow (*e.g.,* making the broker a party to the escrow for the purpose of receiving his or her commission). In addition, any party may authorize an attorney to act on his or her behalf in the escrow. See §15.12.

© The Regents of the University of California

§15.12 C. Attorneys

The buyer's and the seller's attorneys are not parties to the escrow and are not entitled to give instructions to the escrow holder or to amend the buyer's or the seller's instructions, unless the attorney's client expressly authorizes it. *Moss v Minor Props*. (1968) 262 CA2d 847, 69 CR 341. In commercial transactions, the parties typically empower the attorney to prepare escrow instructions, but this is less common in residential transactions.

The attorney acts in concert with the other professionals involved in the transaction but is the only competent adviser on the transaction's legal consequences and, unlike the brokers, escrow holder, title officer, and lender, has no conflicting interest in advising his or her client. The brokers may greatly assist in obtaining details about the property, such as contracts, leases, rent rolls, and tenant estoppel certificates. The escrow holder may provide information on customary escrow procedures and prorations. The title officer will advise on the form of the expected title insurance policy and endorsements. Lenders will sometimes provide loan documents for the attorney's review. The attorney must be part of the team but also act independently to ensure that the interests of the client are protected.

The attorney for a party to an escrow owes a duty of professional care to his client but not to the escrow holder. *St. Paul Title Co. v Meier* (1986) 181 CA3d 948, 226 CR 538.

© The Regents of the University of California

§15.13 D. Lenders

The lender may be a party to an escrow if the transaction involves new financing. The conditional deposit of loan funds in connection with escrow instructions creates an escrow, making the lender a party to the escrow. *Money Store Inv. Corp. v Southern Cal. Bank* (2002) 98 CA4th 722, 120 CR2d 58. In addition to traditional lenders, the seller may be involved in financing the transaction. An escrow may also involve the seller's existing lender, but that lender is not a party to the escrow if its only involvement is receiving the payment of an existing encumbrance and eliminating a lien from the property. *Summit Fin. Holdings, Ltd. v Continental Lawyers Title Co.* (2002) 27 C4th 705, 117 CR2d 541. Customarily, the escrow holder will request a pay-off demand (CC §2943), in which the lender states the amount required to repay the loan and provides the escrow holder with a reconveyance of the existing lien for use on payment of the demand amount. New financing often results from the activities of a mortgage loan broker, who is also not a party to the escrow. The mortgage loan broker ordinarily arranges for compensation directly with the lender, and not through escrow.

NOTE: Until January 1, 2014, beneficiaries of deeds of trust must prepare and deliver a short-pay demand statement within 21 days of receiving a short-pay request from an entitled person. The short-pay statement must set forth an amount less than the outstanding debt, together with any terms and conditions, under which the beneficiary will execute and deliver a reconveyance of the deed of trust. A beneficiary who elects not to proceed with the proposed transaction may refuse to provide a short-pay demand statement but must provide a written statement within 21 days indicating that it has elected not to proceed with the transaction. CC §2943. For more on short sales, see chap 6.

On title instructions for loan transactions, see also California Title Insurance Practice §§10.16-10.17 (2d ed Cal CEB 1997).

© The Regents of the University of California

§15.14 E. Brokers

The real estate brokers for the buyer and the seller are not parties to the escrow, and thus are not entitled to give or amend instructions on behalf of the buyer or the seller without the express authority of a party to the escrow.

Brokers routinely submit demands to escrow for payment of their commissions, often in the form of an irrevocable assignment of the seller's proceeds. See §15.94. Such a demand makes the broker a party for the sole purpose of payment of the commission. An assignment of proceeds by a party to the escrow is enforceable by the broker against the escrow holder. See *Builders' Control Serv. v North Am. Title Guar. Co.* (1962) 205 CA2d 68, 22 CR 712.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.15 F. Title Insurer

§15.15 F. Title Insurer

Title insurance companies are regulated by the state of California and licensed by the California Department of Insurance to issue title insurance. Ins C §§12340-12417. Title insurers issue the policies that buyers and lenders customarily obtain during a purchase or refinance of real property. The title insurer may be the same entity as the escrow holder, it may be a sister company, it may be an underwriter for the escrow company, or it may be unrelated to the escrow company. See California Title Insurance Practice (2d ed Cal CEB 1997) for further discussion of title insurance and title insurance companies.

Most title insurers have sister companies that handle escrows. In Northern California, most of the escrow holders handling real property transactions are either sister companies of a title insurer or part of an underwritten title company. Underwritten title companies are agents for the title insurers and are also regulated and licensed by the California Department of Insurance. There is a contract between the title insurer and the underwritten agent that defines the relationship between the two companies. The underwritten agent is authorized under the contract to issue the policies of the underwriter.

In Southern California, independent escrow companies handle many escrows. Those independent escrow companies place orders for title insurance with title insurance companies or their underwritten agents. Independent escrow companies are unrelated to the title insurance company.

The title insurer is involved in each transaction because the parties to the escrow require a policy at closing. The parties will instruct the escrow holder on which items in a preliminary report are acceptable as exceptions in the policy. The escrow holder will then clear the items that the parties are not willing to accept as exceptions in the policy (generally the seller's liens).

© The Regents of the University of California

III. FUNCTIONS OF ESCROW HOLDER

§15.16 A. Generally

The escrow holder's functions are straightforward: to strictly follow the instructions of the parties to the escrow. Escrow holders incur no liability for failing to do something that is not required by the escrow instructions. *Lee v Title Ins. & Trust Co.* (1968) 264 CA2d 160, 70 CR 378; *Blackburn v McCoy* (1934) 1 CA2d 648, 37 P2d 153. For further discussion of escrow holders' liability, see §§15.22-15.25.

Once the escrow is opened (see §15.7), the escrow officer orders a preliminary report from the title department or a title insurer. The escrow officer arranges for the delivery of the preliminary report to the parties, their brokers, and their attorneys. The escrow officer then initiates the actions necessary to effectuate a close of escrow.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.17 B. Residential Transactions

§15.17 B. Residential Transactions

In a typical residential escrow the escrow, holder does the following:

- Receives the initial deposit and any additional deposits;
- Prepares escrow instructions explaining the conditions for recording the deed and disbursing funds;
- Gives any notices required by law;
- Handles forms and funds if necessary for California tax withholding (see §§15.75-15.79);
- Handles forms and funds if requested for Foreign Investment in Real Property Tax Act of 1980 (FIRPTA) (see §§15.80-15.84);
- Orders demands from existing lenders and lien holders;
- Prepares the deed;
- If requested, prepares the note and deed of trust;
- Obtains loan documents from the new lender;
- Distributes documents among the parties and between the buyer and the lender;
- Meets with the buyer and the seller to have them sign escrow instructions and any documents necessary to complete the escrow;
- Arranges for the borrower to sign loan documents;
- Arranges for the notarization of documents (usually, the escrow officer is also a notary public; on notary's duties, see CC §§1181-1183.5, 1196-1197);
- Obtains demands from the brokers;
- Obtains lien releases and reconveyances for recording;
- Prepares an estimated settlement statement for approval;
- Orders the funds from the lender;
- Prepares recording instructions for the title department or title company;
- Sends the documents to the designated person in the title department or at the title company for recording;
- Releases funds on confirmation of recording; and
- Notifies the parties that the transaction has closed.

© The Regents of the University of California

IV. ESCROW HOLDER'S DUTIES

§15.18 A. Limited Agency

An escrow creates a limited agency relationship between the escrow holder and the parties to the escrow. *Rianda v San Benito Title Guar. Co.* (1950) 35 C2d 170, 217 P2d 25; *Kirby v Palos Verdes Escrow Co.* (1986) 183 CA3d 57, 64, 227 CR 785, disapproved on other grounds in *Summit Fin. Holdings, Ltd. v Continental Lawyers Title Co.* (2002) 27 C4th 705, 712, 117 CR2d 541. This dual agency requires the escrow holder to carry out the instructions of all of the parties to the escrow. *Vournas v Fidelity Nat'l Title Ins. Co.* (1999) 73 CA4th 668, 674, 86 CR2d 490. An escrow holder must comply strictly with the instructions of the parties. *Amen v Merced County Title Co.* (1962) 58 C2d 528, 25 CR 65; *Siegel v Fidelity Nat'l Title Ins. Co.* (1996) 46 CA4th 1181, 54 CR2d 84; *Claussen v First Am. Title Guar. Co.* (1986) 186 CA3d 429, 230 CR 749. An escrow holder incurs no liability either for failing to do something not required by the escrow's terms or for doing something required by the escrow instructions. See *Summit Fin. Holdings, Ltd. v Continental Lawyers Title Co.* (2002) 27 C4th 705, 117 CR2d 541. For a detailed discussion of *Summit,* see Bernhardt & Whitman, *Summit Financial Holdings Redux*, 25 CEB Real Prop L Rep 126 (May 2002). Absent clear evidence of fraud, the escrow holder's obligations are limited to compliance with the instructions of the parties. *Lee v Title Ins. & Trust Co.* (1968) 264 CA2d 160, 162, 70 CR 378.

The escrow holder is the agent of both parties until the time of closing. Thus, when a deed is deposited by a seller and money is deposited by a buyer, the escrow holder is the agent of both parties until all closing conditions are met. Then the escrow holder becomes the agent of each party—of the buyer regarding the deed and of the seller regarding the money. *Shreeves v Pearson* (1924) 194 C 699, 230 P 448.

Instructions may be oral, written, or both. *Zang v Northwestern Title Co.* (1982) 135 CA3d 159, 185 CR 176. Generally, instructions may be modified or revoked until the time of closing. This right to modify or revoke the instructions is not fatal to formation of a contract between a party and the escrow holder. In *Money Store Inv. Corp. v Southern Cal. Bank* (2002) 98 CA4th 722, 120 CR2d 58, the escrow holder argued that a party's reservation of the right to withdraw or amend rendered any contract illusory. The court disagreed, pointing out that partial performance by a party makes the contract enforceable. If the escrow closes, a reservation of the right to modify instructions does not prevent a suit for breach of the escrow contract. But see *Contemporary Invs. v Safeco Title Ins. Co.* (1983) 145 CA3d 999, 193 CR 822.

If the parties submit ambiguous, conflicting, or erroneous instructions, the escrow holder has a duty to clarify the questionable instructions before closing the escrow. *Kirk Corp. v First Am. Title Co.* (1990) 220 CA3d 785, 270 CR 24.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.19 B. Fiduciary Responsibilities

§15.19 B. Fiduciary Responsibilities

The escrow holder is also a fiduciary of each of the parties. *Amen v Merced County Title Co*. (1962) 58 C2d 528, 25 CR 65; *Common Wealth Ins. Sys., Inc. v Kersten* (1974) 40 CA3d 1014, 115 CR 653. Thus, the escrow holder must act in good faith and perform its duties with the ordinary skill of an escrow holder. The fiduciary duty of an escrow holder is usually satisfied by faithful compliance with the instructions of the parties. *Hannon v Western Title Ins. Co.* (1989) 211 CA3d 1122, 260 CR 21.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.20 C. Disclosures to Parties

§15.20 C. Disclosures to Parties

Under the general rules of agency, matters learned by an agent are imputed to its principal because the agent has a duty to disclose them to the principal. CC §2332. In other words, imputation is based on the assumption that the agent will do its duty and will communicate to its principal material matters learned in the course of the agency. *Early v Owens* (1930) 109 CA 489, 293 P 136. However, because the escrow holder is the agent of both the buyer and the seller, this imputation rule is limited in the escrow context. Obviously, this dual agency is fraught with potential for conflicts of interest between or among the parties to the escrow. These potential conflicts are most often avoided because the escrow holder will require mutual and consistent instructions before closing.

As a limited agent (see §15.18), the escrow holder has a duty to disclose material matters that would have a substantial adverse effect on the principal when the escrow holder knows the principal is relying on the agent for protection as to those facts. *Marriage of Cloney* (2001) 91 CA4th 429, 110 CR2d 615; *Kirby v Palos Verdes Escrow Co.* (1986) 183 CA3d 57, 227 CR 785, disapproved on other grounds in *Summit Fin. Holdings, Ltd. v Continental Lawyers Title Co.* (2002) 27 C4th 705, 712, 117 CR2d 541. In *Cloney,* the escrow officer, acting as the notary, learned while acknowledging the seller's signature on the deed that the seller, "Mike Cloney," was also known as "James Michael Cloney." As a result, a recorded judgment against James Michael Cloney (and properly indexed) became constructive notice to the buyer because of the escrow officer's actual knowledge of the fact that Mike Cloney and James Michael Cloney were one and the same. Ordinarily such a difference in names would mean that a judgment against one name would not attach to the title of property held in the other name. See *Orr v Byers* (1988) 198 CA3d 666, 244 CR 13 (no constructive notice provided by abstract of judgment incorrectly spelling name of judgment debtor).

Matters *actually* known by the agent, however, will be imputed to the principal as *constructive notice* regardless of whether they are actually communicated.

NOTE: This is directly contrary to the rule between the title insurer and its insured. There is no imputation to the insured of knowledge acquired by the title insurer in the course of its underwriting or searching of title. *Rice v Taylor* (1934) 220 C 629, 32 P2d 381; *Mayhew v Burke* (1929) 206 C 396, 274 P 517; *Lewis v Superior Court* (1994) 30 CA4th 1850, 37 CR2d 63.

Knowledge obtained in one of two separate escrows will not be imputed to parties in another escrow who were not also parties to the first. *La Mancha Dev. Corp. v Sheegog* (1978) 78 CA3d 9, 144 CR 59; *Far W. Sav. & Loan Ass'n v McLaughlin* (1988) 201 CA3d 67, 246 CR 872. This is true even if the two escrows are not separated by time. The rule against imputation between escrows is not based on whether someone may actually recall the information from one escrow to another or whether the same escrow officer might have handled both. Thus, even simultaneous escrows handled by the same escrow officer are protected from imputation of information between them when the party from whom information is to be imputed is not a party to the same escrow as the party to whom the information is material. *Triple A Mgmt. Co. v Frisone* (1999) 69 CA4th 520, 81 CR2d 669.

The escrow holder has no duty to give advice about the propriety of the transaction for either principal. *Cunningham v Security Title Ins. Co*. (1966) 241 CA2d 626, 50 CR 724.

© The Regents of the University of California

§15.21 D. Duty to Disclose Fraud

The dual agency relationship makes disclosure of fraud particularly difficult. The general rule is that the escrow holder has no duty to disclose that one principal is committing a fraud on the other principal; thus, this information will not be imputed to the defrauded principal. *Lee v Title Ins. & Trust Co.* (1968) 264 CA2d 160, 70 CR 378. However, the escrow holder has a fiduciary duty to the defrauded party and should not participate in a fraud. *Moe v Transamerica Title Ins. Co*. (1971) 21 CA3d 289, 98 CR 547.

Because an escrow holder is a fiduciary, a party to the escrow has a "relaxed" duty of diligence to discover a fraud that may toll the limitations period, and is entitled to assume the escrow holder is properly following the party's instructions. *Lee v Escrow Consultants, Inc*. (1989) 210 CA3d 915, 259 CR 117. Although the issue in *Lee v Escrow Consultants* concerned accrual of a statute of limitations, the court also discussed the nature of an escrow holder's duty. The escrow holder's conduct to which the plaintiff-buyer objected was the disbursement of funds to the seller before the transfer of title to the plaintiff. The escrow holder made the premature disbursement on the receipt of a written amendment to the escrow instructions on which the plaintiff's signature was allegedly forged. The escrow holder argued that, because escrow holders do not have a duty to go beyond the escrow instructions and notify the parties of suspicious facts or circumstances (*Lee v Title Ins. & Trust Co., supra*), it had no duty to investigate the validity of an amendment that, on its face, seemed proper. The court distinguished *Lee v Title Ins. & Trust Co., supra,* however, holding that the original escrow instructions required that changes to the escrow instructions be "given in a writing by all parties," and that the escrow holder thus had a duty to verify the signatures on a purported amendment to the instructions. *Lee v Escrow Consultants, Inc*. (1989) 210 CA3d 915, 924, 259 CR 117. See also *Romo v Stewart Title* (1995) 35 CA4th 1609, 1619, 42 CR2d 414 (court reversed summary judgment, permitting plaintiff to proceed with suit against escrow agent whose alleged fraud and negligence resulted in plaintiff's losing commissions paid to broker).

PRACTICE TIP: If the escrow holder learns of a potential fraud that should be disclosed, a conflict arises with the escrow holder's duty to the other principal. As a result, escrow should stop without disclosure and the escrow holder should refuse to go forward.

© The Regents of the University of California

V. LIABILITY OF ESCROW HOLDER

§15.22 A. Liability to Parties to Escrow

If a party to an escrow suffers damages proximately caused by the escrow holder, the escrow holder may be held liable for damages in contract or in tort. A breach of the escrow contract may result in damages. *Amen v Merced County Title Co.* (1962) 58 C2d 528, 25 CR 65. Likewise, an escrow holder may be responsible for any damages caused by negligence in performing its duties. *Common Wealth Ins. Sys., Inc. v Kersten* (1974) 40 CA3d 1014, 115 CR 653. The measure of damages and the statute of limitations may differ depending on the theory pursued.

In an action for breach of contract, the measure of damages is generally "the amount which will compensate the party aggrieved for all the detriment proximately caused thereby, or which, in the ordinary course of things, would be likely to result therefrom." CC §3300. In an action for negligent performance, the measure of damages is generally "the amount which will compensate for all the detriment proximately caused thereby, whether it could have been anticipated or not." CC §3333.

The statute of limitations for breach of contract is 4 years for a written contract and 2 years for an oral contract. CCP §§337, 339. For negligent performance, the limitations period is 4 years if the escrow instructions were written (*Bruckman v Parliament Escrow Corp*. (1987) 190 CA3d 1051, 235 CR 813), and 2 years if the instructions were oral (*Amen v Merced County Title Co*. (1962) 58 C2d 528, 25 CR 65). A tort cause of action accrues on the discovery of the negligence. *Iusi v City Title Ins. Co*. (1963) 213 CA2d 582, 28 CR 893.

In one case, an escrow holder was held liable on a cross-complaint for implied contractual indemnity for failure to record a declaration of restrictions, contrary to instructions. *Bear Creek Planning Comm'n v Title Ins. & Trust Co.* (1985) 164 CA3d 1227, 211 CR 172, disapproved on other grounds in *Bay Dev., Ltd. v Superior Court* (1990) 50 C3d 1012, 1032, 269 CR 720.

The escrow holder will be liable to any injured party for intentional tortious conduct, such as conversion or embezzlement of escrow funds by the escrow holder, or, on proper proof, for slander of title. *Stalberg v Western Title Ins. Co*. (1994) 27 CA4th 925, 32 CR2d 750; *Stalberg v Western Title Ins. Co.* (1991) 230 CA3d 1223, 282 CR 43 (escrow holder recorded fictitious easement on behalf of upstream owners, affecting plaintiffs' downstream properties).

An escrow holder may have a relationship with the parties to an escrow that would subject the escrow holder to liability for sexual harassment if the elements of CC §51.9 are present.

© The Regents of the University of California

§15.23 B. Liability to Nonparties

The escrow holder may also be liable to nonparties affected by an escrow transaction. Such liability may be based on a third party beneficiary theory or a negligence theory. *Money Store Inv. Corp. v Southern Cal. Bank* (2002) 98 CA4th 722, 120 CR2d 58. For example, an escrow holder may be held liable to an assignor of sales proceeds for failing to follow an instruction by a party to the escrow to remit the proceeds to the assignee on the close of escrow. *Builders' Control Serv. v North Am. Title Guar. Co*. (1962) 205 CA2d 68, 22 CR 712. By contrast, a third party assignee has no such claim against an escrow holder if the assignor is not a party to the escrow. In *Summit Fin. Holdings, Ltd. v Continental Lawyers Title Co.* (2002) 27 C4th 705, 712, 117 CR2d 541, the court refused to impose liability on the escrow holder when a nonparty assigned its loan to another nonparty and the escrow holder paid the assignor as instructed by a party. The court distinguished *Builders' Control Serv. v North Am. Title Guar. Co., supra,* and *Contemporary Invs. v Safeco Title Ins. Co.* (1983) 145 CA3d 999, 193 CR 822, and disapproved *Kirby v Palos Verdes Escrow Co.* (1986) 183 CA3d 57, 227 CR 785.

In Southern California, it has become common for the title company to act as a sub-escrow for a lender, receiving funds and documents to pay off an existing deed of trust in the process of recording a new deed of trust from the new lender. The new lender submits instructions and is thus a party to the sub-escrow, but the borrower-owner is not a party, despite some incidental benefit. In *Markowitz v Fidelity Nat'l Title Co.* (2006) 142 CA4th 508, 48 CR3d 217, the court did not directly address the legality of the sub-escrow practice, and thus did not explicitly resolve the issue of whether a sub-escrow is an escrow independent from the primary escrow being handled by the lender relating to the new loan. In holding that the borrower was not a party to the sub-escrow, however, the court seemed to presume the independent nature of a sub-escrow.

The escrow holder may be liable if a creditor relies on the escrow holder's promise to pay but, because of a party's amended instruction, the escrow holder does not pay the demand. To avoid potential liability based on the creditor's reliance, the escrow holder should notify the creditor of the changed circumstance. *Feinberg v Intrastate Escrow Corp.* (1963) 216 CA2d 80, 30 CR 781.

Punitive damages may be recovered from an escrow holder, but only on proof of malice, fraud, or oppression by the escrow holder. *Flyer's Body Shop Profit Sharing Plan v Ticor Title Ins. Co*. (1986) 185 CA3d 1149, 230 CR 276.

© The Regents of the University of California

§15.24 C. Accommodation Recordings

As a courtesy, escrow holders may agree to record a document (not prepared by the escrow holder) on behalf of a party to an escrow without assuming any liability for the consequences; this is referred to as an "accommodation recording." Brokers, principals, and attorneys all find it convenient to ask escrow for this service, even when there is no pending escrow to which the documents may relate.

Unfortunately, this service can result in liability for the effect of the recorded document. In *Seeley v Seymour* (1987) 190 CA3d 844, 237 CR 282, an optimistic potential tenant prepared a memorandum of agreement setting forth the essential terms of a lease that had not been signed by the landlord, the owner of the property. The title company agreed to record the memorandum, although it was signed only by the potential tenant. The title company delivered the memorandum to the county recorder for recording along with other documents to be insured by the title company. In the ensuing litigation, the title company was held liable for slander of title. The court held that it was not a defense that the memorandum had been recorded as an accommodation to the potential tenant. The court held that the title company had a duty to the landlord-owner of the property, based partly on the foreseeability of economic harm to the owner that would result from the recording.

Escrow may limit its liability by obtaining accommodation instructions. The party who requests the recording may be asked to indemnify the escrow holder against any harm arising from the recording of the document. *Rooz v Kimmel* (1997) 55 CA4th 573, 64 CR2d 177.

© The Regents of the University of California

§15.25 D. Escheat

Escheat is the procedure by which the state takes title to property when the true owner cannot be located. CCP §1300(c). Under the Unclaimed Property Law (CCP §§1500-1582), the escrow holder must comply with the procedures to notify the owners of the lack of activity regarding any unclaimed funds and to eventually deliver those funds to the state. Escrow holders must file an annual report with the State Controller and transfer funds that have escheated. CCP §1530. Once the escrow holder delivers the funds to the State Controller, the escrow holder is relieved of all liability concerning the funds. CCP §1560. A prime source of unclaimed funds is money held after the close of escrow pending further instructions from the parties.

© The Regents of the University of California

VI. DEPOSIT INTO ESCROW AND ITS CONSEQUENCES

§15.26 A. Conditional Delivery

The delivery to a third party of funds or documents (*e.g.,* a grant deed or a deed of trust) to be delivered to another on the performance of a condition creates an escrow (see §15.7). CC §1057. When the condition is satisfied, the escrow holder delivers the documents or money to the appropriate parties, according to instructions.

Escrow is made necessary because a grant deed takes effect only on its delivery, which cannot be conditional. The seller will not want to deliver the grant deed until payment is received, but cannot avoid the effect of delivery of the grant deed directly to the buyer. Thus, the seller must rely on escrow to deliver the grant deed to the buyer when the buyer deposits the necessary funds. CC §§1054, 1056.

Funds that have been deposited into escrow subject to a condition will be released on satisfaction of the condition in accordance with escrow instructions or the terms of the purchase agreement. Most purchase agreements provide for liquidated damages to the seller if the transaction fails to close because of the buyer's default. See §4.142.

When neither party tenders performance sufficient to close the escrow, so that neither party is in default, the right to cancel the escrow and obtain the deposit will depend on the terms of the purchase agreement and the conduct of the parties. See *Galdjie v Darwish* (2003) 113 CA4th 1331, 7 CR3d 178 (seller waived a "time of the essence" clause by her conduct and had no right to cancel escrow).

Conflicts among the parties about the release of funds or documents may result in an interpleader of the funds or documents by the escrow holder. See §15.98.

PRACTICE TIP: An attorney who receives documents or funds from an opposing party under conditional authority to use them becomes an escrow holder. *Wasmann v Seidenberg* (1988) 202 CA3d 752, 248 CR 744. In the event of a conflict between the attorney's client and the opposing party as to the disposition of the documents or funds, the attorney should interplead the documents or funds. *Virtanen v O'Connell* (2006) 140 CA4th 688, 44 CR3d 702. See §§15.2-15.6.

© The Regents of the University of California

B. Effect on Title and Possession

§15.27 1. Before Conditions Are Satisfied

Title to items deposited in escrow will depend on whether the conditions of their deposit have been satisfied. Before the conditions are satisfied, title to any item deposited in escrow remains with the party who deposited it. That is, the buyer or lender retains title to funds deposited, and the seller retains title to and possession of the property and any documents the seller deposited into escrow. *Love v White* (1961) 56 C2d 192, 14 CR 442.

Title is important in determining who bears the risk of loss if property is destroyed. See CC §1662. Similarly, the risk of loss of the funds falls on the party who has title to the funds at the time of the loss. For example, an embezzlement by the escrow holder before closing is the buyer's or lender's loss. *Hildebrand v Beck* (1925) 196 C 141, 236 P 301. By contrast, if all of the conditions of the escrow have been satisfied, the title to the funds passes to the seller, and any embezzlement after that time is the seller's loss. *Greenzweight v Title Guar. & Trust Co.* (1934) 1 C2d 577, 36 P2d 186. Embezzlements by escrow holders may entitle the parties to seek recovery under Fin Code §§17310-17315.

Finally, title to deposits determines when a creditor can acquire a lien on money or property a debtor will receive at the close of escrow or when a commission or other demand may be paid from proceeds. Until title passes, the money is still the buyer's and the property is still the seller's. Thus, a creditor of the buyer cannot acquire a lien on the property and a creditor of the seller cannot reach the purchase money until the escrow closes. For a further discussion of risk of loss under the Uniform Vendor and Purchaser Risk Act (CC §1662) and the ability to modify the allocation of risk of loss by contract, see §§4.137, 13.3-13.14.

Any premature delivery by the escrow holder to the other party is a void transfer that does not pass title to the recipient. *Greenzweight v Title Guar. & Trust Co*. (1934) 1 C2d 577, 36 P2d 186. For example, a seller can quiet title to the property if the grant deed was delivered to the buyer before payment of the purchase price, and a buyer can recover the purchase money from the seller if it was delivered prematurely. *Kish v Bay Counties Title Guar. Co*. (1967) 254 CA2d 725, 62 CR 494. The escrow holder is liable for any loss caused by such premature delivery or return.

© The Regents of the University of California

§15.28 2. After Conditions Are Satisfied

When the conditions of escrow are satisfied, title to deposits in escrow passes to the other party regardless of whether the escrow holder has actually delivered them. *Hagge v Drew* (1945) 27 C2d 368, 165 P2d 461; *Andover Land Co. v Hoffman* (1968) 264 CA2d 87, 70 CR 38. The actual closing of escrow occurs when all of the conditions are satisfied, not when the escrow holder has actually delivered funds or documents.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.29 3. Waiver of Conditions

§15.29 3. Waiver of Conditions

A party may waive an unsatisfied condition and allow the close of escrow. When all conditions have been satisfied or waived, title will be transferred, and escrow will close. *Kish v Bay Counties Title Guar. Co*. (1967) 254 CA2d 725, 62 CR 494.

© The Regents of the University of California

§15.30 VII. THIRD PARTY DEMANDS

One of the most difficult situations that can arise in an escrow involves a conflicting instruction between a party to the escrow and a third party. The interrelationship between escrow and title makes it crucial for everyone involved to understand who are the parties to the escrow (see §§15.9-15.15) and how the third party's demand affects closing the transaction.

Third parties who are not parties to the escrow but who make a demand for payment through the escrow may include the following:

- Judgment creditors;
- Judgment lien holders;
- Attorneys for the parties;
- Brokers, for purposes other than collecting commissions;
- The Internal Revenue Service;
- The Franchise Tax Board; and
- The seller's lender.

All of these parties are strangers to the escrow. Generally escrow cannot take instructions from these nonparties unless a party (usually the seller) tells escrow to pay the demand of the nonparty. It is common for the seller to instruct escrow to pay the liens that encumber the property. Payment to the nonparties who have an interest encumbering the real property is usually a buyer's requirement for closing the transaction. The buyer and the buyer's lender are usually unwilling to accept property that remains subject to the seller's liens.

Even though the creditors are not parties to the escrow, once the escrow holder has agreed to pay a third party creditor, the escrow holder must avoid acting in a negligent manner and can be liable to the third party creditor if payment is not properly made. For example, the escrow holder may be liable for paying the wrong party. *Warington Lumber Co. v Fullerton Mortgage & Escrow Co.* (1963) 222 CA2d 706, 35 CR 423.

A stranger to the escrow can become a party to the escrow through an assignment of proceeds by the seller. This procedure is common for real estate broker commissions. See §15.94. Any creditor can obtain an assignment of proceeds from the seller. Once the escrow holder is notified of the assignment, the assignee becomes a party to the escrow for the purpose of receiving the funds. If the escrow holder then receives amended escrow instructions from the assignor-seller that conflict with the demand of the assignee creditor, the escrow holder would have to hold or interplead the funds. See §15.98. *Builders' Control Serv. v North Am. Title Guar. Co.* (1962) 205 CA2d 68, 22 CR 712.

© The Regents of the University of California

VIII. ESCROW INSTRUCTIONS

§15.31 A. General Provisions

Escrow companies draft general provisions to cover the generic issues that arise in every escrow. Often, statutorily required notices are printed as a part of the general provisions, *e.g.,* privacy notice (15 USC §6801; 16 CFR pt 313) and California withholding notice (Rev & T C §18668; see §15.75). In a commercial transaction, parties often negotiate amendments to some of the instructions found in the general provisions. For a sample of general provisions, see App S.

The most common general provisions that are negotiated in a commercial transaction relate to the escrow company's attempt to limit liability (paragraph 7 in App S) and to alternative dispute resolution (paragraph 12 in App S). Attorneys often merely delete those paragraphs completely from the general provisions. In larger commercial transactions the escrow might not include general provisions. Instead, every detail may be drafted to satisfy the requirements of the parties to the transaction.

General provisions often contain an attorney fees provision for specific issues related to payment of escrow fees and costs (paragraph 11 in App S). In *Kangarlou v Progressive Title Co.* (2005) 128 CA4th 1174, 27 CR3d 754, the court interpreted those limited attorney fees provisions as applying to the entire contract. The plaintiff had purchased property using the defendant's escrow services and then sued the escrow holder for breach of fiduciary duty and attorney fees. The general provisions of the escrow instructions provided for the escrow holder to receive attorney fees and costs incurred in a collection action against a party to the escrow for failure to make payments to the escrow holder. The court determined that although the escrow holder attempted to limit attorney fees under CC §1717(a), the attorney fees provision applied to the entire contract. Plaintiff was able to recover the attorney fees. But see *Paul v Schoellkopf* (2005) 128 CA4th 147, 26 CR3d 766 (provision limiting attorney fees to those incurred by company in collecting for escrow services did not apply to disputes between buyer and seller over land sale contract).

PRACTICE TIP: Escrow holders often include various exculpatory clauses in the general provisions. Some escrow holders insist that these clauses be incorporated into any individually prepared instructions submitted to them. Each party's attorney must analyze these clauses carefully to see whether any important protections or rights are being waived. Exculpatory clauses that purport to relieve the escrow agent of any liability are often unenforceable. *Akin v Business Title Corp*. (1968) 264 CA2d 153, 159, 70 CR 287. But see *Rooz v Kimmel* (1997) 55 CA4th 573, 64 CR2d 177, for an example of a broad escrow exculpatory and indemnity clause that was found to be enforceable when the escrow company agreed to record a deed of trust as an accommodation and without commercial benefit, but negligently failed to do so in a timely fashion. Typical exculpatory provisions are discussed in §15.24.

© The Regents of the University of California

§15.32 B. California Association of Realtors® Contract

In 2000, the California Association of Realtors® (CAR) adopted a new form, the Residential Purchase Agreement and Joint Escrow Instructions (CAR Contract). The CAR Contract, currently in use in most California counties, has been revised several times since its creation. The most interesting feature of the CAR Contract for escrow purposes is the inclusion of joint escrow instructions in the residential purchase agreement. A copy of the CAR Contract is in §6.24.

Before adoption of the CAR Contract (and currently, in counties where the CAR Contract is not used), the escrow holder would draw escrow instructions—unique to each transaction—on the basis of information provided by the parties or the broker. The escrow holder would generally not receive a copy of the purchase agreement between the buyer and the seller. The instructions would cover all of the conditions for close of escrow, the division of costs and fees, and a list of other tasks to be performed by the escrow holder.

Paragraph 28 of the CAR Contract lists those paragraphs in the CAR Contract that constitute the joint escrow instructions. Paragraph 28 makes it clear that the escrow holder is not to be concerned with paragraphs other than those listed. Paragraph 28 also provides that the escrow holder will send a copy of the general provisions to the parties, and if the general provisions conflict with the provisions of the CAR Contract, the general provisions will control. On the general provisions, see §15.31.

The CAR Contract provides that it is to be given to the escrow holder within 3 days after acceptance by the seller. The escrow holder acknowledges receipt of the CAR Contract and any deposit in writing, and by signing the CAR Contract agrees to act as the escrow holder subject to paragraph 28. If there are any issues that are not addressed in the CAR Contract or if there are any ambiguities in the CAR Contract that relate to the escrow holder's responsibilities, the escrow holder will draft supplemental instructions to address those issues. For a form of buyer's supplemental instructions, see §§15.50-15.61; for a form of seller's supplemental instructions, see §§15.63-15.73. Some escrow officers have not accepted the CAR Contract and continue to draft full escrow instructions for signature by the parties.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.33 C. Preparation of Escrow Instructions

§15.33 C. Preparation of Escrow Instructions

Sections 15.34-15.47 discuss certain legal and practical issues that arise in drafting supplemental escrow instructions for the buyer or the seller. Supplemental instructions are seldom used if the California Association of Realtors® Residential Purchase Agreement and Joint Escrow Instructions (CAR Contract) is used. The CAR Contract contains most of the escrow instructions that are customarily needed in a residential transaction. Before drafting any additional instructions, counsel should review the CAR Contract to ascertain whether additional instructions are necessary. Most items that are unique to the specific transaction can be addressed in paragraph 25, "Other Terms and Conditions" (see §6.24 for copy of CAR Contract). Supplemental instructions should clarify any ambiguity found in the CAR Contract. Generally, the escrow officer will draft brief specific instructions that relate to any ambiguities or areas that are not addressed in the CAR Contract.

© The Regents of the University of California

§15.34 1. Property Description

Early in the transaction the attorney should confirm that the preliminary report accurately describes the property. If the legal description is too complicated for counsel to accurately locate, a surveyor can be hired to verify the legal description and to locate any easements and exceptions on a survey or plat.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/ 2. Deposit of Funds/§15.35 a. Good Funds Law

2. Deposit of Funds

§15.35 a. Good Funds Law

California's "good funds" laws (see Ins C §12413.1) require advance planning in order to fund escrow in sufficient time to achieve the agreed closing date. Payment in the form of cashier's, certified, or teller (association) checks allows the escrow holder to close and funds to be disbursed on the day after deposit into the escrow account, regardless of the state in which the account is located. Personal checks require significantly more time.

PRACTICE TIP: The parties, wishing to maximize their return on funds, often want to deposit funds on the same day as the funds are to be disbursed. This can happen only if the deposit is cash or a wire transfer to the escrow account of the escrow holder. When planning a same-day transfer, attorneys and parties must be aware of the wire transfer time limits of banks and title companies and differing time zones. Finally, attorneys and parties should consult early with the escrow holder concerning its requirements for funding before releasing documents for recording. Ordinarily, the escrow holder will require that funds arrive earlier than close of business on the day before the date the parties intend the documents to be recorded.

© The Regents of the University of California

§15.36 b. Right of Escrow Holder to Commingle Funds

Escrow holders deposit funds into a common escrow account. They do not maintain individual accounts for each escrow transaction. The general provisions (see §15.31) of the escrow holder's form instructions disclose this practice. Generally, funds are held for such a brief period of time that the cost of setting up an individual account is higher than the amount of interest the party may receive on funds in a separate account. The depositing party should analyze the cost and benefit of segregating funds if funds are to remain with escrow for more than a few days.

PRACTICE TIP: When dealing with an underwritten title company (*i.e.,* an agent of a title insurance company—not an insurer), depositors should consider obtaining a closing protection letter from the prospective title insurer concerning the escrow agent's closing activities. Generally, in the closing protection letter the title insurer protects the parties against the underwritten title company's fraud, defalcation, or improper handling of documents or payments. For further discussion of closing protection letters, see California Title Insurance Practice §3.5 (2d ed Cal CEB 1997). Alternatively, a lender may wish to arrange a sub-escrow by which the title company handles funds but the escrow company handles documents and accounting functions.

© The Regents of the University of California

§15.37 c. Interest on Deposits

An escrow holder has no duty to deposit funds held in escrow in an interest-bearing account. *Hannon v Western Title Ins. Co*. (1989) 211 CA3d 1122, 260 CR 21. A party who wants funds to earn interest should instruct the escrow holder accordingly.

© The Regents of the University of California

§15.38 3. Drafting Documents

Conveyance and loan documents may be drafted by the parties or their attorneys, by the lender, or, in residential transactions, by the escrow holder. If the escrow holder drafts any documents, the seller must provide the specific terms and approve the form before the buyer executes them. If the seller is represented by counsel, the seller's counsel may draft the loan documents; if the escrow holder drafts them, the seller's counsel should review them.

Title companies will provide a list of the documents that the escrow holder may draft, and may list them on their website. (An escrow holder's responsibilities with respect to obtaining a valid conveyance of title are discussed in *Marriage of Cloney* (2001) 91 CA4th 429, 110 CR2d 615. For a further discussion of *Cloney*, see §15.20.)

© The Regents of the University of California

§15.39 4. Leases

If the buyer is purchasing the property subject to leases, the purchase agreement should describe how the seller will transfer the leases to the buyer. On purchase subject to leases, see §4.73. The seller's interest in the leases will be transferred to the buyer, and the buyer will formally assume the lease obligations, by use of an assignment and assumption of leases. The seller should also be required to deliver the original lease to the buyer on or before the closing. The escrow holder will deliver leases deposited by the seller but will want to avoid any responsibility for ensuring the validity or enforceability of the delivery or the assignment. The tenants must be notified of the assignment in order to ensure receipt of rent by the buyer.

Additionally, the purchase agreement generally provides that the buyer will receive and approve tenant estoppel certificates. The original estoppel certificates may be delivered to the buyer directly or through escrow. Also, an institutional lender will normally require a subordination, nondisturbance, and attornment agreement from the tenants. See Retail Leasing: Drafting and Negotiating the Lease, chap 44 (Cal CEB 2007); Office Leasing: Drafting and Negotiating the Lease, chap 28 (Cal CEB 1996).

© The Regents of the University of California

§15.40 5. Title Insurance

Negotiations for the form and contents of a title policy are conducted with the title company or the title department if the escrow holder is affiliated with a title insurance company. See §15.2. During a pending transaction, for example, attorneys may wish to delete certain exceptions listed in the preliminary report, have liens removed, relocate easements, or amend declarations of restrictions. These discussions will usually involve only the title company and not the escrow holder. For an in-depth discussion of preliminary reports, various title policies, and the many endorsements available, see California Title Insurance Practice (2d ed Cal CEB 1997). For form of escrow instructions regarding title insurance requirements, see §15.53.

NOTE: The title insurer will often ask the seller to sign an affidavit providing information an owner of property would know that a title insurer would not. The title insurer uses the information to eliminate certain title insurance risks, such as recent construction at the property, occupants of the property, easements or encroachments, access rights, disputes about use of the land, or supplemental taxes. Normally, the seller is obligated to the buyer by contract to deliver clear title by arranging and paying for a title insurance policy acceptable to the buyer. By completing the affidavit for the title insurer, the seller saves the increased charges a title insurer would incur to inspect the property. Depending on the insurance requested, the seller may choose not to assume liability for answering certain questions on the affidavit. Alternatively, the seller may request the title insurer to make its own inspection, although such a request requires advance notice to the title company.

There is often a delay of days or weeks after closing before the title insurance policy is sent to the insured, or insured's counsel. As a result, it is important that counsel review the issued policy to confirm that it conforms to the policy requested in the escrow instructions. Particular attention should be paid to the vesting, legal description, exceptions listed in Schedule B, and any requested endorsements. Any error of the title company should be promptly corrected. Failure to bring to the insurer's attention errors in the policy issued may bind the insured to the coverage that was issued. See *Hallmark Ins. Co. v Superior Court* (1988) 201 CA3d 1014, 247 CR 638.

© The Regents of the University of California

§15.41 6. Executing and Delivering Documents

In residential transactions, documents are usually executed at the escrow office. Because the title company will insure the validity and enforceability of deeds, easements, and deeds of trust recorded through escrow, the title company will want to control the signing and attaching of notarial acknowledgements to minimize exposure under the contemplated title policy for fraud, undue influence, capacity, and forgery. On fraud, see §15.21.

Escrow instructions should clearly identify to whom all documents are to be delivered because escrow holders are reluctant to deliver documents that are not clearly identified by both parties. In most cases, the escrow holder will not deliver keys, security passes, or similar items.

© The Regents of the University of California

§15.42 7. Closing; Closing Costs

When selecting a closing date, the parties must be aware that county recorders have special times for recording by title companies, usually first thing in the morning. This allows the title company to review the previous day's recordings to be sure that nothing will adversely affect the transaction being recorded. Some counties allow title companies to record later during the day, as a "special recording." Counsel should not assume that this is an option but should check with the county where the documents are to be recorded to ascertain whether special recordings are allowed. On closing, see §4.132.

The purchase agreement should clearly allocate between the parties all closing costs, including escrow and title fees, loan fees, transfer taxes, attorney fees, and broker's commissions. Each county in California has a "customary" allocation of such costs, and the custom may be determined by reviewing the websites of the major title insurers, or by asking local real estate brokers. On closing costs, see §§4.134-4.135.

© The Regents of the University of California

§15.43 8. Prorations

The allocation of charges between the buyer and the seller as of the closing date is called proration. The purchase agreement usually addresses this division of amounts paid or received by the seller or the buyer that would benefit the other party before or after the closing date. If the seller makes expenditures before closing that benefit the buyer after the closing date (*e.g.,* property taxes for a period that ends after the closing; see §15.44), the seller is entitled to a credit for the amount by which the buyer will benefit, after closing, from the expenditure. Similarly, if the buyer makes expenditures after closing that in retrospect benefited the seller before the closing date, the buyer is entitled to a credit for the amount by which the seller benefited, before closing, from the expenditure.

PRACTICE NOTE: The purchase agreement will often provide that any items that were not readily susceptible to proration or were incorrectly prorated will be balanced by the parties and reimbursed within a short time after the closing date.

The most common types of prorations include real property taxes and assessments (§15.44), insurance premiums (§15.45), and rent (§15.46). For a further discussion of prorations, see §4.133.

© The Regents of the University of California

§15.44 a. Real Property Taxes and Assessments

Real property taxes are billed in two installments for each tax year (July 1 through June 30). For example, if a sale transaction closes in March, and both installments have been paid, the seller has paid taxes through June 30 of the current tax year that are properly the responsibility of the buyer after the closing date.

PRACTICE TIP: Parties and their attorneys should also be aware of escape and supplemental assessments. If there has been recent construction on the property or if ownership has recently been transferred, the tax assessor may not have completed the task of reassessing the property to reflect such matters. After the close of escrow, the tax assessor may issue an escape assessment (Rev & T C §531) or supplemental assessment (Rev & T C §531.2), and this possibility should be handled in the purchase agreement.

If the property lies within certain special assessment districts, these assessments must also be prorated. These special assessments should be disclosed as exceptions in the preliminary report. Special assessments are collected with real property taxes and should be reflected on the latest tax bill for the property.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.45 b. Insurance Premiums

§15.45 b. Insurance Premiums

If the seller assigns any insurance policies to the buyer, the premiums must be prorated as of the closing or other date chosen by the parties. If the seller intends to cancel insurance policies, and the buyer will obtain its own insurance, the seller may be entitled to a premium refund for the period after closing. See §§4.106, 13.98 for discussion of hazard insurance. On property insurance in general, see chap 13.

© The Regents of the University of California

§15.46 c. Rent

The escrow holder should be instructed to transfer to the buyer any rent from the property collected by the seller that is attributable to the period after the closing, including any security deposits paid to the seller by the tenant. CC §§1950.5, 1950.7. Other lease-related charges that may need to be prorated are expenses that the landlord pays but which are periodically reimbursed by a tenant (rather than paid directly by the tenant). Examples include maintenance charges, utilities, taxes, and insurance.

In commercial retail transactions, tenants may be paying percentage rent, based on sales, sometimes in advance, with provisions for periodic adjustments. All of these items should be prorated, and that may be accomplished in escrow.

See §4.133 for discussion of the various methods that buyer and seller can use to manage the issue of delinquent rent. See §4.73 for discussion of tenant estoppel certificates and App K for a form.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.47 9. Recordation; Priority

§15.47 9. Recordation; Priority

The buyer's attorney should carefully consider the order of priority for recording documents at the closing. For example, if a new or amended declaration of restrictions is to be recorded, the attorney should make sure that the signer of the declaration holds title when it is recorded. If the declaration is signed by the buyer, the conveyance to the buyer must be recorded before the declaration. The title officer (not the escrow officer) may be able to assist the parties and their attorneys in determining the order of priority.

© The Regents of the University of California

§15.48 IX. SUPPLEMENTAL ESCROW INSTRUCTIONS TO PURCHASE AGREEMENT AND JOINT ESCROW INSTRUCTIONS

Even when the parties use the California Association of Realtors® (CAR) form Residential Purchase Agreement and Joint Escrow Instructions (see §6.24), the parties need to provide supplemental escrow instructions. Sections 15.50-15.61 contain a form of buyer's supplemental escrow instructions, and §§15.63-15.73 contain a form of seller's supplemental escrow instructions. Section 15.74 discusses the lender's supplemental escrow instructions in a residential transaction.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.49 A. Buyer's Supplemental Escrow Instructions

§15.49 A. Buyer's Supplemental Escrow Instructions

The buyer's objective is to deposit funds in exchange for title to the purchased property. Thus, the buyer's instructions should identify the conditions to the escrow holder's delivery of the buyer's funds to the seller. The form in §§15.50-15.61 identifies the buyer's deposits, conditions to delivery, and the procedure for closing the escrow.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.50 1. Form: Introduction

§15.50 1. Form: Introduction

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.50-15.61.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

15.50-1 Introduction

Buyer's Escrow Instructions

_ _[*Date*]_ _

TO: _ _[*name and address of escrow holder*]_ _

Your Escrow No. _ _ _ _ _ _ _ _

Our File No. _ _ _ _ _ _ _ _

Transaction: _ _[*name of seller*]_ _ **to** _ _[*name of buyer*]_ _

Property: _ _[s*treet address or APN*]_ _

This letter shall constitute the escrow instructions of _ _[*name*]_ _ **, Buyer, for the purchase from** _ _[*name*]_ _**, Seller, of the real property described in** _ _[*your/name of title company*]_ _ _ _[*preliminary report/pro forma title policy/title commitment*]_ _ **dated** _ _[*date*]_ _**, Order No.** _ _ _ _ _ _ _ _**.**

Comment: The introduction states the information necessary to identify the transaction and the party providing the escrow instructions. The escrow and order numbers may be the same if escrow and title services are provided by the same company. See §15.15. However, if the buyer works with a national title service office, or if the escrow and title offices are in different counties or states, the numbers will probably differ. All relevant numbers should be referenced to avoid confusion.

In describing the transaction, refer to any exchange parties that will be involved. There may be an accommodator for either the buyer or the seller, or both. In such cases, reference to "Buyer" or "Seller" may be ambiguous. Instead, the drafter should create short names for the parties and accommodators that will minimize confusion. For a detailed discussion of exchanges, see Real Property Exchanges (3d ed Cal CEB 2002).

If no street address has been assigned to the property to be purchased, the correct assessor's parcel number(s) may be used instead of a street address.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.51 2. Form: Deposits by Buyer

§15.51 2. Form: Deposits by Buyer

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.50-15.61.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

15.51-1 Deposits by buyer

A. Buyer deposits the following into escrow:

1. _ _[*Funds/Cashier's check, payable to your order/wire transfer, according to your transfer instructions*]**_ _, in the amount of _ _**[*dollar amount*]**_ _;**

2. Resolutions by Buyer's _ _[*directors/members/managers*]**_ _;**

[*If applicable, add one or both of the following options*]

[*Option 1: Third party financing*]

3. Promissory note in the principal amount of _ _[*dollar amount*]**_ _, payable to _ _**[*name of lender*]**_ _;**

4. Deed of trust and assignment of rents in favor of _ _[*name of lender*]**_ _, as beneficiary;**

5. _ _[*Add any other primary loan documents*]**_ _;**

[*Option 2: Seller financing*]

[6.] Promissory note in the principal amount of _ _[*dollar amount*]**_ _, payable to _ _**[*name of seller*]**_ _;**

[7.] Deed of trust and assignment of rents in favor of _ _[*name of seller*]**_ _, as beneficiary;**

[8.]_ _[*Add any other primary loan documents*]**_ _;**

[*Continue*]

[9.] Preliminary change of ownership report.

Any additional funds required to be deposited by Buyer in order to close this escrow will be deposited within _ _[*number*]**_ _ days of receipt of written notice from escrow holder stating the amount due.**

Comment: This clause identifies the funds and documents deposited by the buyer. The instructions should also list any additional loan documents or disclosures required by either an institutional lender or by the seller as lender and should clearly state the number of originals and counterparts deposited.

The amount of funds required is derived from the purchase price less any deposits by the buyer, increased or decreased by closing costs and prorations. On prorations, see §4.133; for escrow instructions provision, see §15.57.

© The Regents of the University of California

§15.52 3. Form: Conditions Precedent to Close of Escrow

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.50-15.61.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

15.52-1 Conditions precedent to close of escrow

B. You are hereby authorized to close the above-referenced transaction in accordance with these instructions when, and only when, all of the following conditions have been fully satisfied:

1. You have received the grant deed to Buyer _ _[*or Buyer's chosen entity or accommodator*]**_ _, in a form approved by Buyer, duly executed and acknowledged by Seller, as grantor;**

[*If appropriate, add one or more of the following*]

2. You hold for Buyer the original of the lease, dated _ _[*date*]**_ _, by and between _ _**[*name*]**_ _, as landlord, and _ _**[*name*]**_ _, as tenant, for the premises located at _ _**[*address*]**_ _, reviewed and approved by Buyer. Please obtain an Assignment and Assumption of Lease(s), in the form approved by Buyer, and executed and _ _**[*add, if to be recorded: notarially acknowledged*]**_ _ by Seller and Buyer;**

[3.] Bill of Sale (for personal property), _ _[*executed/to be executed*]**_ _ by Seller;**

[4.] All original books, records, plans, specifications, leases, and other documents of Seller, as identified in section _ _ of the purchase agreement; and

[5.] One (1) original of each of the Federal and State of California Nonforeign Withholding Affidavits, executed by Seller.

[6.] You shall have dated all documents as of the date of closing, unless otherwise dated.

Comment: On transfer of leases, see §15.39.

If the seller is transferring any personal property to the buyer as part of the transaction, a bill of sale should be prepared that identifies the personal property.

On federal and state nonforeign withholding affidavits, see §§15.75-15.84.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.53 4. Form: Title Insurance Requirements

§15.53 4. Form: Title Insurance Requirements

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.50-15.61.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

15.53-1 Title insurance requirements

[7.]_ _[*You are unconditionally prepared to issue to Buyer your/*_ _[*Name*]_ _ *Title Company has confirmed to you its willingness to issue to Buyer its*]_ _ _ _[*California Land Title Association standard /American Land Title Association extended*]_ _ **coverage owner's policy of title insurance,** _ _[*in the exact form of the preliminary report/pro forma/title commitment attached to this letter,*]_ _ **in the amount of** _ _[*the purchase price*]_ _**, insuring that** _ _[*e.g., fee*]_ _ **title to the real property described in the** _ _[*preliminary report/pro forma/title commitment*]_ _ **is vested in** _ _[*Buyer or Buyer's designated entity and manner of holding title*]_ _**, including without limitation** _ _[*list any endorsements requested by Buyer*]_ _**. All title exceptions, other than exceptions** _ _[*list by number or describe*]_ _ **in the** _ _[*preliminary report/pro forma/title commitment*]_ _**, must be eliminated before the Closing.**

Comment: This instruction obligates the escrow holder to obtain the requested title insurance policy. Ordinarily, the amount of coverage for the title policy will be determined by the purchase price. However, a buyer who intends to construct substantial improvements should consider obtaining endorsements to increase policy limits as improvements are completed, or persuading the title insurer that a higher policy limit, based on the anticipated value of the improvements, is justified.

Standard exceptions to title include taxes, recorded easements, deeds of trust, declarations of restrictions, and other recorded documents affecting title. The exceptions that the buyer will permit in the title policy should be listed by number according to the preliminary report. If a preliminary report is not yet available, the escrow instructions should be amended when it is available. Otherwise, the permitted title exceptions must be clearly described, including recording information. It is also acceptable to attach to the escrow instructions a marked-up version of the preliminary report or commitment. Any documents to be recorded through escrow at the closing should be authorized as exceptions, *e.g.,* any new deed of trust, easement, or declaration of restrictions.

NOTE: A pro forma title insurance policy will show the exact form of the contemplated title policy, including endorsements. A title commitment or preliminary report will show the title exceptions as of the date of the report or commitment but not the endorsements.

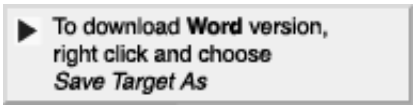
If the buyer is obtaining financing to help purchase the property, the lender will submit instructions stating the lender's title insurance requirements. See §15.74.

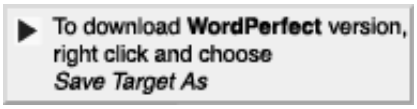
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.54 5. Form: Estimated Closing Statement

§15.54 5. Form: Estimated Closing Statement

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.50-15.61.





15.54-1 Estimated closing statement

[8.] You shall have prepared and delivered to Buyer an estimated closing statement for this transaction, reflecting all charges, costs, and fees to be paid by _ _[*Buyer/accommodator*]_ _ and all other disbursements and the recipients thereof, and after approval of such estimated closing statement, you shall have telephonically advised _ _[*Buyer/Buyer's counsel*]_ _ of any change in the closing statement and received telephonic approval of any such change.

Comment: The escrow holder will draft an estimated closing statement for review by the parties to the escrow. Each party's statement will show only that party's side of the transaction, but the escrow holder cannot draft the statements until both sides have provided sufficient information. The statement should be carefully reviewed by both counsel and client to be sure the instructions regarding prorations and costs have been followed. For a form good faith estimate, see App X; on the good faith estimate form, see §15.95.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.55 6. Form: Procedure for Closing

§15.55 6. Form: Procedure for Closing

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.50-15.61.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

15.55-1 Procedure for closing

C. When you have fulfilled all of the conditions specified under _ _[*e.g., section B*]_ _ above, you shall close this escrow by performing the following steps in the manner, within the time periods, and in the order specified:

1. Record in the appropriate Official Records the following documents in the following order of priority:

a. The grant deed;

b. The deed of trust;

[*If applicable, add one or more of the following options*]

[*Option 1: Seller financing*]

c. The Seller's deed of trust;

[*Option 2: Seller is assigning one or more leases to buyer*]

[d.] The assignment of leases; and

_ _[*if applicable, other loan documents, such as Subordination, Nondisturbance, and Attornment Agreements*]_ _.

[*Continue*]

2. Disburse all funds in accordance with the approved estimated settlement statement and these instructions.

3. Deliver one (1) original of each of the following documents to _ _[*Buyer/Buyer's counsel/Buyer and Buyer's counsel*]_ _**: a certified copy of the grant deed, a certified copy of the deed(s) of trust, assignment of leases, _ _**[*list other relevant documents*]_ _**, and copies of each of the loan documents and the nonforeign affidavits.**

[*If appropriate, add*]

4. Deliver to _ _[*accommodator*]_ _ **certified copies of all of the documents described in _ _**[*e.g., section C1*]_ _**, in such manner as _ _**[*accommodator*]_ _ **may direct.**

[*Continue*]

[5.] Within _ _[*number of days/hours*]_ _ **of closing, deliver to _ _**[*Buyer/Buyer's counsel/Buyer and Buyer's counsel*]_ _ **certified copies (including recording information) of the deed of trust, _ _**[*add any additional recorded documents to go to Buyer, e.g., assignment of rents, subordination, nondisturbance, and attornment agreement/any other recorded documents*]_ _**, and a copy of the preliminary change of ownership report; and deliver to _ _**[*Buyer/Buyer's counsel*]_ _ **the owner's title policy.**

[6.] Within _ _[*number of days/hours*]_ _ **of closing, deliver to _ _**[*Buyer/Buyer's counsel/Buyer and Buyer's counsel*]_ _ **one (1) certified copy of final closing statements prepared by you and consistent with the approved estimated closing statement.**

Comment: On priority, see §15.47. On the estimated closing statement, see §15.54.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.56 7. Form: Time for Closing Escrow; Investment of Funds

§15.56 7. Form: Time for Closing Escrow; Investment of Funds

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.50-15.61.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

15.56-1 Time for closing escrow; investment of funds

D. If you are unable to close this escrow immediately on receipt of funds deposited by _ _[*Buyer/accommodator*]_ _**, you are then authorized and instructed to invest the funds** _ _[*describe choice of investment*]_ _ **until the escrow closes or these instructions are revoked by Buyer. Such investments shall be made through a national or state banking institution reasonably acceptable to you. All interest earned on invested funds shall accrue solely to the account of Buyer until the escrow closes, when this interest earned shall become the property of Buyer. If either this escrow does not close by** _ _[*date*]_ _ **or these instructions are revoked by Buyer, then the funds and all interest earned on the funds shall be promptly returned to the parties from whom such funds were originally received by you.**

Comment: The time limit on closing escrow is usually based on the purchase agreement. The parties usually specify the date that the documents should be recorded in the official records. The escrow may close, if all conditions are satisfied, by the close of business the day before the documents are recorded. Thus, in the unfortunate situation that the buyer dies during the night after all conditions were satisfied, escrow has still closed and the documents should be recorded the next day. On closing, see §§4.132-4.136, 15.42.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.57 8. Form: Prorations

§15.57 8. Form: Prorations

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.50-15.61.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

15.57-1 Prorations

E. You shall prorate the following items between Buyer and Seller on the basis of a 30-day month as of _ _[*the close of escrow/specify date*]_ _**:**

1. Real property taxes relating to the property for the fiscal year _ _[*year*]_ _ **through** _ _[*year*]_ _ **according to the most recent information available from the taxing authority.**

2. Insurance premiums relating to the property.

[*If applicable, add one or both of the following options*]

[*Option 1: Rents prorated*]

3. Rents collected relating to the property, as disclosed by the _ _[*tenant estoppel certificates/rent roll*]_ _ **deposited into escrow by Seller, together with the balance of any security deposit paid by each tenant.**

[*Option 2: Insurance policies assigned*]

[4.] The premiums relating to the following insurance policies to be assigned to Buyer by Seller: _ _[*identify policies*]_ _

[*Continue*]

Comment: The purchase agreement should address the division between the buyer and the seller of amounts paid or received by the seller or the buyer that would benefit the other party before or after the closing date. The escrow instructions should accurately reflect this agreement. On prorations, see §§4.133, 15.43-15.46.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.58 9. Form: Authorized Disbursements; Costs

§15.58 9. Form: Authorized Disbursements; Costs

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.50-15.61.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

15.58-1 Authorized disbursements; costs

F. Buyer shall pay one-half of your escrow fees, the excess cost of the premium for the owner's ALTA title insurance policy over the cost of the premium for a CLTA owner's policy (and the lender's CLTA or ALTA title insurance policy, if applicable), the cost of any endorsements Buyer requests to its title policy, and the fees for any notary services provided to Buyer.

[*If appropriate, add*]

Seller shall pay one-half of your escrow fees, the cost of the premium for the owner's CLTA title insurance policy (or joint protection policy, if Seller financing), any real estate broker's commissions, the cost of clearing and delivering title according to the purchase agreement, and the cost of preparing and delivering the grant deed.

[*Continue*]

Comment: The allocation of closing costs, including the escrow and title fees, should be negotiated and agreed in the purchase agreement. Often the seller will agree to pay the premium for a California Land Title Association (CLTA) standard coverage policy, as provided in the above form. If the buyer requests an American Land Title Association (ALTA) extended coverage owner's title policy, then the buyer will pay the difference between the premium for the CLTA policy and the premium for the ALTA policy. As borrower, the buyer will also pay for the lender's title policy. The escrow instructions' allocation between the parties of the costs of closing, including escrow and title fees, loan fees, transfer taxes, attorney fees, and broker's commissions, should reflect the allocations made by the purchase agreement. On closing costs, see §§4.134, 15.42.

For clarification, the buyer may add the second paragraph, which confirms the fees and costs payable by the seller, although the buyer may not commit the seller to actually pay them. The seller must submit a matching instruction. For a form, see §15.69.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.59 10. Form: Right to Withdraw Documents or Funds

§15.59 10. Form: Right to Withdraw Documents or Funds

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.50-15.61.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

15.59-1 Right to withdraw documents or funds

G. Buyer reserves the right to withdraw any or all documents or funds from this escrow submitted under these escrow instructions at any time before the close of this escrow.

Comment: Similar language was held not fatal to formation of a contract between a party and the escrow holder in *Money Store Inv. Corp. v Southern Cal. Bank* (2002) 98 CA4th 722, 120 CR2d 58; see §15.18.

The parties' rights to withdraw documents or funds are not unilateral, but governed by their contract and their conduct during performance. See *Galdjie v Darwish* (2003) 113 CA4th 1331, 7 CR3d 178 (seller waived "time of the essence" clause by repeated failure to insist on buyer's timely performance and therefore had no right to cancel escrow, even though closing date stated in purchase agreement had passed). Similarly, a party may lose the right to cancel a sale and be forced by a court to close escrow when that party has interfered with the other party's ability to perform a condition to closing. See *Peak-Las Positas Partners v Bollag* (2009) 172 CA4th 101, 90 CR3d 775 (affirming judgment of specific performance extending escrow); *Ninety Nine Invs., Ltd. v Overseas Courier Serv. (Singapore) Private, Ltd.* (2003) 113 CA4th 1118, 6 CR3d 891 (seller's conduct prevented buyer from timely obtaining a loan to close escrow). On specific performance with additional discussion of *Peak-Las Positas*, see §4.149. In the event of a dispute between the parties regarding the funds on deposit in escrow, the escrow holder's general instructions usually provide that the escrow holder may interplead the funds. On interpleader, see §15.98.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.60 11. Form: Document Approval

§15.60 11. Form: Document Approval

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.50-15.61.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

15.60-1 Document approval

[*Add one of the following alternatives*]

[*Alternative 1: Buyer's silence deemed approval*]

H. If these instructions require the approval by Buyer of any report, statement, form, or other document, approval shall be considered given if Buyer has not given written notice of disapproval to you of any such item or items within _ _[*number*]_ _ days after you notify Buyer of receipt of the item and you furnish Buyer with a copy of that item.

[*Alternative 2: Buyer's silence deemed disapproval*]

H. If these instructions require the approval by Buyer of any report, statement, form, or other document, approval shall be considered given if Buyer has notified you in writing stating such approval of any such item or items within _ _[*number*]_ _ days after you notify Buyer of receipt of the item and you furnish Buyer with a copy of that item. If Buyer fails to notify you within such _ _[*number*]_ _-day period, Buyer shall be deemed to have disapproved such item.

[*Continue*]

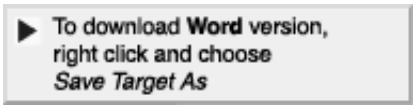
Comment: Alternative 1 provides that the buyer may passively approve items requiring the buyer's approval as a condition to closing. However, counsel should consider whether it is preferable that inaction by the buyer be deemed disapproval. If so, Alternative 2 should be used. Obviously, for the escrow to proceed, the approval method required must be consistent with the other parties' instructions.

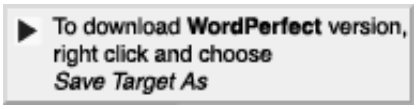
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.61 12. Form: Acknowledgment by Escrow Holder

§15.61 12. Form: Acknowledgment by Escrow Holder

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.50-15.61.





15.61-1 Acknowledgment by escrow holder

Please acknowledge your receipt of these instructions, and your agreement to act as escrow agent in connection with the above-described transactions in accordance with these instructions, by executing and dating a copy of this letter where indicated below and returning it to the undersigned.

Very truly yours,
__[*Signature of attorney*]__

By our signature below, we acknowledge receipt of these instructions and all enclosures specified in these instructions, and we agree to act as escrow agent in these transactions in accordance with these instructions.

Date: _ _ _ _ _ _ _ _[*ESCROW OR TITLE COMPANY*]_ _

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

Comment: Counsel should ascertain well in advance whether instructions will be accepted from counsel without the signature of the party represented. See §15.12.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.62 B. Seller's Supplemental Escrow Instructions

§15.62 B. Seller's Supplemental Escrow Instructions

The seller's objective is to deposit the deed in exchange for the agreed purchase price. Thus, the seller will identify the conditions to the escrow holder's delivery of the deed to the buyer. The form in §§15.63-15.73 identifies the seller's deposits, conditions to delivery, and the procedure for closing the escrow.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.63 1. Form: Introduction

§15.63 1. Form: Introduction

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.63-15.73.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

15.63-1 Introduction

Seller's Escrow Instructions

_ _[*Date*]_ _

TO: _ _[*name and address of escrow holder*]_ _

Your Escrow No. _ _ _ _ _ _ _ _

Our File No. _ _ _ _ _ _ _ _

Transaction: _ _[*name of seller*]_ _ **to** _ _[*name of buyer*]_ _

Property: _ _[s*treet address or APN*]_ _

This letter shall constitute the escrow instructions of _ _[*name*]_ _**, Seller, for the sale to** _ _[*name*]_ _**, Buyer, of the real property described in** _ _[*your/name of title company*]_ _ _ _[*preliminary report/pro forma title policy/title commitment*]_ _ **dated** _ _[*date*]_ _**, Order No.** _ _ _ _ _ _ _ _**.**

Comment: On this introductory language, see Comment in §15.50.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.64 2. Form: Deposits by Seller

§15.64 2. Form: Deposits by Seller

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.63-15.73.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

15.64-1 Deposits by seller

A. Seller deposits the following into escrow:

1. Grant Deed to _ _[*Buyer/Buyer's entity/accommodator*]_ _, _ _[*executed/to be executed*]_ _ and acknowledged by Seller, as grantor;

2. Resolutions by _ _[*Seller's directors/members/managers*]_ _;

[*If applicable, add one or more of the following options*]

[*Option 1: Seller is providing financing*]

3. Promissory note in the principal amount of _ _[*dollar amount*]_ _, payable to _ _[*Seller*]_ _, to be signed by Buyer as borrower;

4. Deed of trust and assignment of rents in favor of _ _[*Seller*]_ _, as beneficiary, to be signed and acknowledged by Buyer as trustor;

[*Option 2: Seller is assigning lease*]

[5.] Rent statement;

[6.] The original of the lease(s), dated _ _[*date*]_ _, by and between _ _[*name*]_ _, as landlord, and _ _[*name*]_ _, as tenant, for the premises located at _ _[*address*]_ _;

[7.] Tenant letter, notifying the tenant of the assignment and assumption of leases, to be dated as of the closing date.

[*Option 3: Seller is transferring personal property*]

[8.] Bill of Sale (for personal property), _ _[*executed/to be executed*]_ _ by Seller;

[*Option 4: Seller is delivering books, records, leases, or other documents*]

[9.] All original books, records, plans, specifications, leases, and other documents of Seller, as identified in section _ _ of the purchase agreement; and

[*Continue*]

[10.] One (1) original of each of the Federal and State of California Nonforeign Withholding Affidavits.

[11.] Owner's affidavit, as requested by title insurer.

Comment: This clause identifies the documents deposited by the seller. Any additional loan documents or disclosures should also be listed. The instructions should clearly state the number of originals and counterparts that are deposited. On drafting documents, see §15.38. See also comments in §§15.51-15.52. On federal and state nonforeign withholding affidavits, see §§15.75-15.84.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.65 3. Form: Conditions Precedent to Close of Escrow

§15.65 3. Form: Conditions Precedent to Close of Escrow

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.63-15.73.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

15.65-1 Conditions precedent to close of escrow

B. You are authorized to close the above-referenced transaction in accordance with these instructions when, and only when, all of the following conditions have been fully satisfied:

1. You hold for Seller's account cash or other form of available funds (including the _ _[*amount*]**_ _ previously deposited by Buyer into this escrow) sufficient to pay the Purchase Price (as defined in the purchase agreement) and all closing costs, expenses, and prorations for which Buyer is responsible _ _**[*less the amount of the promissory note referenced in paragraph, e.g., A3 above*]**_ _.**

2. You have received the promissory note and deed of trust in favor of Seller, each executed by Buyer, and acknowledged as appropriate.

3. You have prepared and delivered to Seller a preliminary closing statement for this transaction, reflecting all charges, costs, and fees to be borne by _ _[*Seller/accommodator*]**_ _ and all other disbursements and the recipients thereof, and after approval of such preliminary closing statement, you shall have telephonically advised _ _**[*Seller/Seller's counsel*]**_ _ of any change therein and received telephonic approval of any such change.**

4. You have obtained an assignment and assumption of lease(s), in the form approved by Seller, and executed and _ _[*add, if to be recorded: notarially acknowledged*]**_ _ by Seller and Buyer.**

[*If there is seller financing, add the following option*]

[*Option: Lender's policy*]

5. _ _[*You are unconditionally prepared to issue your/_ _*[*Name*]*_ _ Title Company has confirmed to you its willingness to issue its*]*_ _ _ _*[*California Land Title Association standard/American Land Title Association extended*]*_ _ coverage lender's policy of title insurance, insuring that _ _*[*e.g., fee*]*_ _ title to the real property described in the _ _*[*preliminary report/pro forma/title commitment*]*_ _ is vested in _ _*[*Buyer/Buyer's designated entity and manner of holding title*]*_ _, including without limitation _ _*[*list any endorsements requested by Seller*]*_ _. All title exceptions, other than exceptions _ _*[*list by number or describe*]*_ _ in the _ _*[*preliminary report/pro forma/title commitment*]*_ _, must be eliminated before the Closing.**

[*Continue*]

Comment: The seller's main condition to the delivery of the grant deed to the buyer is receipt of payment of the purchase price. If the seller is also providing financing, the optional language at the end of paragraph 1 should be used.

On the estimated closing statement, see §15.54. For a form good faith estimate, see App X; on the good faith estimate form, see §15.95.

The purchase agreement will describe how any existing leases are to be transferred to the buyer. An assignment and assumption of lease will be required transferring the seller's interest in the leases to the buyer and providing for the buyer's formal assumption of the lease obligations. The original lease(s) should be delivered to the buyer from the seller. The escrow holder will deliver leases deposited by the seller, but will want to avoid any responsibility for ensuring the validity or enforceability of the delivery or the assignment. On assignment, the tenants must be notified of the assignment to ensure receipt of rent by the buyer.

If the buyer is purchasing property subject to leases, the purchase agreement will usually provide that the buyer will receive and approve tenant estoppel certificates. The original estoppel certificates may be delivered to the buyer

through escrow, if desired. Also, an institutional lender will normally require subordination, nondisturbance, and attornment agreements from the tenants. See Office Leasing: Drafting and Negotiating the Lease, chap 28 (Cal CEB 1996).

This provision makes it the escrow holder's obligation to obtain the title insurance policy. Ordinarily, the amount of coverage for the title policy will be determined by the amount of the loan to buyer.

The exceptions that the seller will permit in the title policy should be listed by number according to the preliminary report. If a preliminary report is not yet available, the escrow instructions should be amended when it is available. Otherwise, the permitted title exceptions must be clearly described, including recording information. It is also acceptable to attach to the escrow instructions a marked-up version of the preliminary report or commitment. The seller will normally be required to subordinate to any institutional or individual first lender and the seller's loan policy will reflect the new first deed of trust as an exception.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.66 4. Form: Procedure for Closing

§15.66 4. Form: Procedure for Closing

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.63-15.73.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

15.66-1 Procedure for closing

C. When you have fulfilled all of the conditions specified under _ _[*e.g., section B*]_ _, you shall close this escrow by performing the following steps in the manner, within the time periods, and in the order specified below:

1. Record in the appropriate Official Records the following documents in the following order of priority:

a. The grant deed;

b. The deed of trust;

[*If applicable, add one or more of the following options*]

[*Option 1: Seller financing*]

c. The Seller's deed of trust;

[*Option 2: Seller is assigning one or more leases to buyer*]

[d.] The assignment of leases; and

_ _[*if applicable, other loan documents, such as Subordination, Nondisturbance, and Attornment Agreements*]_ _.

[*Continue*]

2. You shall pay the demand of _ _[*lienholder*]_ _ dated _ _[*date*]_ _.

3. Disburse all funds in accordance with the approved estimated closing statement and these instructions.

4. Date all undated documents as of the date the Grant Deed is recorded in the Official Records.

5. Deliver one (1) original of each of the following documents to _ _[*Seller/Seller's counsel/Seller and Seller's counsel*]_ _: a certified copy of the grant deed, a certified copy of the Seller's deed of trust, the original Seller's promissory note, original assignment of leases, _ _[*list other relevant documents*]_ _, and copies of each of the nonforeign affidavits.

[*If appropriate, add*]

6. Deliver to _ _[*accommodator*]_ _ certified copies of all of the documents described in _ _[*e.g., section C1*]_ _, in such manner as _ _[*accommodator*]_ _ may direct.

[*Continue*]

[7.] Within _ _[*number of days/hours*]_ _ of closing, deliver to _ _[*Seller/Seller's counsel/Seller and Seller's counsel*]_ _ certified copies (including recording information) of the deed of trust, the assignment of leases, and _ _[*add any additional recorded documents to go to Seller*]_ _, _ _[*the cancelled promissory note and deed of trust, per payoff demand*]_ _, and a copy of the preliminary change of ownership report; and deliver to _ _[*Seller/Seller's counsel*]_ _ the Seller's loan policy.

**[8.] Within _ _[*number of days/hours*]_ _ of closing, deliver to _ _[*Seller/Seller's counsel/Seller and Seller's*

counsel]_ _ **one (1) certified copy of final closing statements prepared by you and consistent with the approved estimated closing statement.**

Comment: There is often a delay of days or weeks before the title insurance policy is sent to the insured, or insured's counsel. As a result, it is very important for counsel to review the policy actually issued for its conformity with the policy requested in the escrow instructions. Particular attention should be paid to the vesting, legal description, exceptions listed in Schedule B, and any endorsements attached. Any error of the title company should be promptly corrected. Failure to bring to the insurer's attention errors in the policy issued may bind the insured to the coverage that was issued. See *Hallmark Ins. Co. v Superior Court* (1988) 201 CA3d 1014, 247 CR 638.

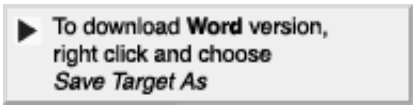
An institutional lender who is being paid to release an existing lien may require that it send the canceled loan documents to the seller directly, outside of escrow, and after receipt of payment in full. In that situation, delete the instruction to escrow to provide the canceled loan documents to the seller at closing.

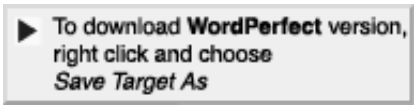
© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.67 5. Form: Time for Closing Escrow

§15.67 5. Form: Time for Closing Escrow

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.63-15.73.





15.67-1 Time for closing escrow

D. You shall close this escrow on or before _ _[*date*]_ _, or these instructions are revoked by Seller and all documents deposited with you by Seller shall be promptly returned to Seller.

Comment: On the time limit on closing escrow and on recording documents, see Comment in §15.56.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.68 6. Form: Prorations; Costs

§15.68 6. Form: Prorations; Costs

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.63-15.73.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

15.68-1 Prorations; costs

E. You shall prorate the following items between Buyer and Seller on the basis of a 30-day month as of _ _[*the close of escrow/specify date*]_ _**:**

1. Real property taxes relating to the property for the fiscal year _ _[*year*]_ _ **through** _ _[*year*]_ _ **according to the most recent information available from the taxing authority.**

2. Insurance premiums relating to the property.

[*Option 1: Rents prorated*]

[3.] Rents collected relating to the property, as disclosed by the _ _[*tenant estoppel certificates/rent roll*]_ _ **deposited into escrow by Seller, together with the balance of any security deposit paid by each tenant.**

[*Option 2: Insurance policies assigned*]

[4.] The premiums relating to the following insurance policies to be assigned to Buyer by Seller: _ _[*identify policies*]_ _

[*Continue*]

Comment: For discussion of prorations and costs, see §4.133 and Comment in §15.57.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.69 7. Form: Authorized Disbursements; Costs

§15.69 7. Form: Authorized Disbursements; Costs

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.63-15.73.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

15.69-1 Authorized disbursements; costs

F. Seller shall pay the documentary transfer tax, one-half of your escrow fees, the cost of the premium for the owner's CLTA title insurance policy (or joint protection policy, if Seller financing), the fees for any notary services provided to Seller, and the recording fees for recording the grant deed.

[*If appropriate, add*]

Buyer shall pay one-half of your escrow fees, the excess cost of the premium for an ALTA title insurance policy, the cost of any endorsements requested by Buyer, the cost of any endorsements Buyer requests to its title policy, and the fees for any notary services provided to Buyer.

[*Continue*]

Comment: The payment of documentary transfer taxes is negotiable, although there are customs in many counties. According to the Revenue and Taxation Code, the seller is liable for such payment. Rev & T C §11912. For further discussion of closing costs, see §§4.134, 15.42.

For clarification, the seller may add the second paragraph, confirming which fees and costs are payable by the buyer, but the seller may not commit the buyer to actually pay them. The buyer must submit a matching instruction. For a form, see §15.58.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.70 8. Form: Payment of Broker's Commission

§15.70 8. Form: Payment of Broker's Commission

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.63-15.73.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

15.70-1 Payment of broker's commission

G. You shall pay from Seller's sales proceeds a real estate broker's commission to _ _[*name(s), address(es) of broker(s)*]_ _ **in the amount of** _ _[*percentage of sales price*]_ _**.** _ _[*Explain any split of the commission.*]_ _

Comment: On real estate broker's commissions, see §15.94.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.71 9. Form: Right to Withdraw Documents or Funds

§15.71 9. Form: Right to Withdraw Documents or Funds

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.63-15.73.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

15.71-1 Right to withdraw documents or funds

H. Seller reserves the right to withdraw any or all documents from this escrow submitted under these escrow instructions at any time before the close of this escrow.

Comment: For discussion of this provision, see Comment in §15.59. On interpleading funds, see §15.98.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.72 10. Form: Document Approval

§15.72 10. Form: Document Approval

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.63-15.73.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

15.72-1 Document approval

[*Add one of the following alternatives*]

[*Alternative 1: Buyer's silence deemed approval*]

I. If these instructions require the approval by Buyer of any report, statement, form, or other document, approval shall be considered given if Buyer has not given written notice of disapproval to you of any such item or items within _ _[*number*]_ _ days after you notify Buyer of receipt of the item and you furnish Buyer with a copy of that item.

[*Alternative 2: Buyer's silence deemed disapproval*]

I. If these instructions require the approval by Buyer of any report, statement, form, or other document, approval shall be considered given if Buyer has notified you in writing stating such approval of any such item or items within _ _[*number*]_ _ days after you notify Buyer of receipt of the item and you furnish Buyer with a copy of that item. If Buyer fails to notify you within such _ _[*number*]_ _-day period, Buyer shall be deemed to have disapproved such item.

[*Continue*]

Comment: See discussion of passive approval and disapproval in Comment in §15.60. The approval method required must be consistent with the other parties' instructions for the escrow to proceed.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.73 11. Form: Acknowledgment by Escrow Holder

§15.73 11. Form: Acknowledgment by Escrow Holder

The form text in this section is part of a larger form. For your convenience, downloading any one of the sections included in the form will download the entire form. The inclusive section numbers are §§15.63-15.73.

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

15.73-1 Acknowledgment by escrow holder

Please acknowledge your receipt of these instructions, and your agreement to act as escrow agent in connection with the above-described transactions in accordance with these instructions, by executing and dating a copy of this letter where indicated below and returning it to the undersigned.

By our signature below, we acknowledge receipt of these instructions and all enclosures specified herein, and we agree to act as escrow agent in these transactions in accordance with the foregoing instructions.

Date: _ _ _ _ _ _ _ _[*ESCROW OR TITLE COMPANY*]_ _

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

Comment: On counsel's ability to provide escrow instructions, see §15.12.

© The Regents of the University of California

§15.74 C. Lender's Instructions

Most institutional residential lenders submit instructions to escrow that are standard forms, preprinted, and not negotiated with the borrower. These instructions are usually accompanied by the lender's prepared loan documents, including the promissory note and deed of trust, and various lender disclosure forms required by different federal and state laws. See Federal Truth in Lending Act (15 USC §§1601-1693r), Real Estate Settlement Procedures Act of 1974 (RESPA) (12 USC §§2601-2617), and CC §§2956-2967. If the lender requests, the escrow holder will supervise the signing of the loan documents by the borrowers. The escrow officer will then act as notary for the borrower's signature on the mortgage or deed of trust.

Commercial lenders will also submit instructions but will usually coordinate drafting instructions and loan documents with the borrower's counsel.

The lender's instructions will require as a condition to closing that the loan documents be fully executed, recorded as appropriate, and returned to the lender. Also, the lender will require a title insurance policy, either in the form of an American Land Title Association (ALTA) lender's policy, a California Land Title Association (CLTA) lender's policy, or in the case of some individual lenders, a CLTA joint protection policy. (See California Title Insurance Practice, chaps 6, 8 (2d ed Cal CEB 1997) for a discussion of lender's title insurance.) Lenders usually also require proof of hazard insurance covering the borrower's property. See chap 13.

Loan funds are normally deposited into escrow by wire transfer once all the other conditions of the lender's instructions have been satisfied, and 1 day before the deed of trust records. A lender may charge the borrower with interest on loan funds deposited into escrow only for 1 day before recording the deed of trust. CC §2948.5.

NOTE: If the proceeds of a loan secured by a deed of trust are to be disbursed on a Monday or the day after a bank holiday, the lender may charge the additional interest that accrues over the weekend or on the bank holiday only if the borrower signs a form disclosing the amount of the extra interest charges accruing and informing the borrower that the extra interest could be avoided by disbursing on a day other than a Monday or the day after a holiday. CC §2948.5. But see *Washington Mut. Bank v Superior Court* (2002) 95 CA4th 606, 115 CR2d 765, holding that CC §2948.5 does not apply to a federally chartered savings and loan association because of federal preemption.

© The Regents of the University of California

X. TAX ISSUES

A. California Withholding

§15.75 1. Withholding Requirements

Revenue and Taxation Code §18662 provides for the withholding of taxes on the disposition of California real estate. The statute requires a prepayment of tax in the amount of 3-1/3 percent of the sales price or the alternative withholding amount unless the seller falls within one of the statutory exemptions from this payment. Rev & T C §18662(e). The buyer is obligated to withhold the amount of tax due at the close of the transaction and send the funds to the Franchise Tax Board. On buyer's obligations, see §15.79. The buyer generally designates the escrow holder to fulfill this obligation to withhold and send the funds.

For many years, only nonindividual sellers were required to document the existence of an exemption or to pay the California withholding tax. Effective January 1, 2003, however, individual sellers who are California residents are also required to either document the existence of an exemption or pay the California withholding tax. Rev & T C §18662(e)(1).

Effective January 1, 2007, sellers who do not qualify for an exemption from California withholding may now choose between two different methods of calculating the amount owed. The standard withholding amount is still 3-1/3 percent of the gross sale price. The alternative withholding amount is based on the maximum tax rate for individuals, banks, and others, as applied to the gain on the sale. The gain on the sale is the difference between the adjusted basis of the property and the amount realized in the sale. Rev & T C §18662(e)(2). The amount realized is the sales price in the current transaction minus the selling expenses. The adjusted basis is determined by starting with the original price that the seller paid for the property. Any points paid by the seller and any depreciation taken are subtracted from the seller's original purchase price. Costs of additions or permanent improvements are added to the seller's original purchase price. That final amount is the adjusted basis.

FTB Form 593-E, Real Estate Withholding—Computation of Estimated Gain or Loss, is used to compute the amount due. See App T. Form 593-E has replaced the former 593-L and is also used to calculate a loss. Form 593-E is signed under penalty of perjury.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.76 2. Individual Exemptions to Withholding Requirements

§15.76 2. Individual Exemptions to Withholding Requirements

The exemptions for individual sellers include the following (Rev & T C §18662(e)(3)):

- The total gross sales price is less than $100,000;
- Certain foreclosures;
- The property is, or was last used as, the seller's principal residence as defined in IRC §121;
- Exchanges under IRC §1031 (except for boot);
- Involuntary conversions as defined by IRC §1033; and
- The sale of the property results in a taxable loss for California tax purposes (the sellers must complete FTB form 593-E, Real Estate Withholding—Computation of Estimated Gain or Loss; see App T).

NOTE: The most common exemption is that the property is the seller's principal residence. Before January 1, 2005, for purposes of this exemption, "principal residence" was defined as the residence occupied by the seller for 2 of the last 5 years (tracking the federal definition under IRC §121). Effective January 1, 2005, an alternative method of qualifying a personal residence was added. The exemption now applies if the property was last used as the seller's principal residence "within the meaning of IRC §121." Rev & T C §18662(e)(3)(D)(i)(II). The Franchise Tax Board forms and publications clarify the apparent ambiguity of that final clause in §18662(e)(3)(D)(i)(II) by adding "without regard to the 2-year time period."

The individual seller signs a declaration (FTB Form 593-C, Real Estate Withholding Certificate; see App U), under penalty of perjury. The form lists all of the exemptions. The seller checks the box that contains the relevant exemption and signs the form. If the seller does not check off a box on this form showing that an exemption applies, the prepayment is due. On the obligation to make this prepayment, see §15.79. All of the forms and instructions can be found on the Franchise Tax Board's website, listed in the Directory.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.77 3. Nonindividual Exemptions to Withholding Requirements

§15.77 3. Nonindividual Exemptions to Withholding Requirements

The exemptions for nonindividual sellers include the following:

- Certain corporations and partnerships (Rev & T C §18662(e)(1));
- Partnerships and limited liability companies;
- Tax-exempt entities, insurance companies, IRAs, and qualified pension plans;
- Estates, but only for sale of the decedent's principal residence; and
- Banks.

Before January 1, 2005, nonindividuals could request a waiver from the required withholding or a reduction in the amount of withholding if the gain from the sale was small. However, as of January 1, 2005, nonindividual sellers can no longer request a waiver or a reduction in withholding. Instead, just like individuals, nonindividuals are either exempt from withholding or must prepay 3-1/3 percent of the total sales price (or the alternative withholding amount). Nonindividuals self-certify an exemption using the same Form 593-C that an individual signs (FTB Form 593-C, Real Estate Withholding Certificate; see App U) declaring under penalty of perjury that the entity falls within one of the statutory exemptions. Former Form 593-W has been eliminated.

© The Regents of the University of California

§15.78 4. No Waiver for Individuals

Under current law there is no complete waiver from withholding for individuals. Thus, even if there are not enough funds to cover the withholding at close, withholding is due. Lack of funds is only relevant if there is a taxable loss on the sale of the property (*i.e.,* basis exceeds sale price). If the seller claims a loss, the seller must also fill out an FTB Form 593-E, Real Estate Withholding—Computation of Gain or Loss. See §15.76; for the form, see App T.

© The Regents of the University of California

§15.79 5. Buyer's Obligations; Penalties

To ensure compliance with the withholding requirement, the legislature has delegated responsibility for withholding to the buyer. The buyer has a right to reasonably rely on the 593-C and 597-W Certifications (see §§15.76-15.77) that are signed under penalty of perjury. Rev & T C §18662(e)(3)(D).

PRACTICE TIP: The buyer should review the certifications before close of escrow. If the certifications are not properly filled out or if they do not make sense, the buyer should clarify the certification with the seller. For privacy protection, sellers should insist that their Social Security numbers be deleted from any forms sent to the buyers.

Special procedures are available for installment sales. Rev & T C §18662(e)(3)(E). If the buyer agrees, the initial withholding amount can be based on the initial payment only and, subsequently, withholding is paid each time an installment payment is made. The buyer must sign a special form (FTB Form 593-I, Real Estate Withholding Installment Sale Agreement) signifying the buyer's agreement to withhold over time.

If funds are due, they must be paid to the Franchise Tax Board by the 20th of the month following the month that title is transferred. Unless the party is a nonindividual requesting a waiver, it is general practice for the escrow holder to send the funds at closing to avoid late penalties. The penalty for failure to withhold is the greater of $500 or 10 percent of the amount due. Rev & T C §18668(d). Generally, the penalty is paid by the buyer. If the escrow holder failed to give the statutory notice regarding withholding, the escrow holder is responsible for the penalty. Rev & T C §18668(e)(1). If the seller knowingly signs a false exemption certificate for the purpose of avoiding the withholding requirements, however, the penalty is the greater of $1000 or 20 percent of the amount due. Rev & T C §18668(e)(5).

© The Regents of the University of California

B. FIRPTA

§15.80 1. Withholding Requirements

The Foreign Investment in Real Property Tax Act of 1980 (FIRPTA) (IRC §§861, 882, 897, 6039C) requires the buyer to withhold 10 percent of the gross sales price paid to a seller who resides in a foreign country unless an exemption applies. See IRC §§897, 1445.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.81 2. Exemptions to Withholding Requirements

§15.81 2. Exemptions to Withholding Requirements

The exemptions to withholding are as follows:

- The sales price of the real property is less than $300,000 and the buyers intend to use the property as their residence. IRC §1445(b)(5).
- The sellers provide the buyers with a nonforeign affidavit, signed under penalty of perjury. There is no official form, but for a sample form, see §15.82; the sellers must state that they are not nonresident aliens and provide their taxpayer identification number and their home address. IRC §1445(b)(2). An individual can obtain a taxpayer identification number quickly from the Internal Revenue Service. IRS Form W-7.

NOTE: The Housing and Economic Recovery Act of 2008 (Pub L 110-289, 122 Stat 2654) added an alternative method for furnishing the nonforeign affidavit to address sellers' concerns regarding identity theft. IRC §1445(b)(9). Under the alternative method, instead of going to the buyer, the nonforeign affidavit is deposited into escrow. The escrow holder then certifies to the buyer that (1) the escrow is the settlement service provider in the transaction, (2) the escrow is not the agent of the seller, (3) the seller has given the nonforeign affidavit to escrow, and (4) the nonforeign affidavit indicates that withholding is not required. The escrow holder is stating that it has the form and that the form indicates that no withholding is required. The escrow holder is *not* certifying the accuracy of the information. The form is kept in the escrow file until the entire escrow file is destroyed.

- The sellers provide the buyers with a notice of nonrecognition of gain or loss. There is no official form; the notice must state the basis for the nonrecognition of gain or loss by reference to an Internal Revenue Code section or treaty, and is signed under penalty of perjury. The buyers send a copy of the notice to the IRS within 20 days after close of escrow. Treas Reg §1.1445-2(d)(2).
- Before the close of escrow, the buyers receive a withholding certificate from the IRS stating that nothing is due. See §15.83.
- The transaction is a gift and the sellers receive no funds. If the sellers are relieved from the liability of a note secured by deed of trust, the sellers have received something of value and withholding is required unless another exemption applies. IRC §1445(b)(5); IRS Form 8288, General Instructions.
- The buyer is the United States or a state of the United States. IRS Form 8288, General Instructions.
- The buyers are acquiring an option. Withholding is required at the time that the option is exercised. IRS Form 8288, General Instructions.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.82 3. Form: Certification of Nonforeign Status by Corporation, Partnership, Trust or Estate

§15.82 3. Form: Certification of Nonforeign Status by Corporation, Partnership, Trust or Estate



CERTIFICATION OF NONFOREIGN STATUS BY CORPORATION, PARTNERSHIP, TRUST OR ESTATE

Section 1445 of the Internal Revenue Code provides that a transferee of a U.S. real property interest must withhold tax if the transferor is a foreign person. For U.S. tax purposes (including section 1445), the owner of a disregarded entity (which has legal title to a U.S. real property interest under local law) will be the transferor of the property and not the disregarded entity. To inform the transferee that withholding of tax is not required upon the disposition of a U.S. real property interest by _____ (hereinafter referred to as "Transferor"), the undersigned hereby certifies the following on behalf of Transferor:

1. Transferor is not a foreign corporation, foreign partnership, foreign trust, or foreign estate (as those terms are defined in the Internal Revenue Code and Income Tax Regulations);

2. Transferor is not a disregarded entity as defined in §1.1445–2(b)(2)(iii);

3. Transferor's U.S. employer identification number is _____; and

4. Transferor's office address is _____
_____.

Transferor understands that this certification may be disclosed to the Internal Revenue Service by transferee and that any false statement contained herein could be punished by fine, imprisonment, or both.

Under penalties of perjury I declare that I have examined this certification and to the best of my knowledge and belief it is true, correct, and complete, and I further declare that I have authority to sign this document on behalf of Transferor.

Date: _____

By: _____

Print Name: _____

Title: _____

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.83 4. Withholding Certificate

§15.83 4. Withholding Certificate

Sellers who take the position that they do not owe withholding, or that they owe less than 10 percent, may request that the IRS reduce the required withholding and determine the maximum tax liability. See IRC §1445(c); Treas Reg §1.1445-3; Rev Proc 2000-35, 2000-1 Cum Bull 211. The sellers would submit an IRS Form 8288-B, Application for Withholding Certificate for Disposition by Foreign Persons of U.S. Real Property Interests. If escrow closes before receipt of a response from the IRS, the 10 percent is held (usually by the escrow holder). If funds are due after the IRS responds, the funds are sent to the IRS within 20 days after the IRS mails the withholding certificate to the buyers. See Treas Reg §1.1445-3; Rev Proc 2000-35.

© The Regents of the University of California

§15.84 5. Buyer's Obligations; Penalties

The buyer is obligated to pay the withholding amounts within 20 days after the close of escrow unless there is a pending application for a withholding certificate. IRS Form 8288, General Instructions. IRS Form 8288, U.S. Withholding Tax Return for Dispositions by Foreign Persons of U.S. Real Property Interests, and IRS Form 8288-A, Statement of Withholding on Dispositions by Foreign Persons of U.S. Real Property Interests, are used to report and send the withholding amount. These forms can be found on the IRS website, which is listed in the Directory. The buyer has a right to reasonably rely on documents submitted by the seller. IRC §1445(b)(7).

PRACTICE TIP: One of the differences between FIRPTA and California withholding (see §§15.75-15.79) is that the escrow holder will not automatically handle all documentation and funds related to FIRPTA unless that is specifically requested by the parties to the escrow. If the seller lives out of the country and FIRPTA withholding may be required, make certain that contingency is clear to all parties who will handle FIRPTA funds and paperwork.

© The Regents of the University of California

XI. CLOSING THE DEAL

§15.85 A. Why Record?

By recording documentation of real property transfers, the buyers and lenders are protected against unknown prior interests in the same property. The recording statutes (CC §§1169-1220; Govt C §§27201-27399) establish that properly indexed and recorded instruments provide notice to all persons of their contents, whether a person looks at them or not, which constitutes so-called constructive notice. In transfers and encumbrances of real property, recording has several effects, including these:

- If the instrument is "recorded as prescribed by law," constructive notice of the contents of the instrument is conclusively presumed. CC §1213 (notice is more fully discussed in §15.86).
- Recording provides actual notice of the instrument's contents to those performing a search of the public records.
- Recording establishes priority of recorded instruments over conveyances and encumbrances that are recorded later, even when the execution of such conveyances and encumbrances was actually earlier in time, as long as the subsequent conveyance was in good faith (*i.e.,* without notice of the prior conveyance) and for valuable consideration. CC §1214.

NOTE: Civil Code §1214 is termed a "race-notice" type of recording statute, as opposed to the "pure race" or "pure notice" types of statutes. The "race" refers to the race to the recorder's office to record an instrument first in time, to meet the "first duly recorded" provision of §1214. "Notice" refers to the fact that the winner of the race must also have no "notice" of any other claim to the interest being transferred. Only with no such "notice" in addition to winning the "race" may the transferee achieve priority of its interest over other purported transfers. In other words, he or she must take his or her interest "in good faith and for a valuable consideration." CC §1214. Notice may be actual or constructive, including imputed or inquiry notice. See §15.86.

© The Regents of the University of California

§15.86 B. Effect of Recording

A conveyance is void against a subsequent conveyance to a bona fide purchaser or bona fide encumbrancer for value who records a conveyance of the same property first. CC §§1107, 1214. See *Hochstein v Romero* (1990) 219 CA3d 447, 268 CR 202. The unrecorded conveyance is still valid between the parties to the conveyance, and those with notice of it. CC §1217. Such "notice" may include actual notice (CC §18(1); *I. E. Assocs. v Safeco Title Ins. Co.* (1985) 39 C3d 281, 216 CR 438) or constructive notice (CC §19), *i.e.,* knowledge of facts that would prompt a reasonable person to inquire further. Thus, a buyer who records the deed and proves its status as a bona fide purchaser for value without notice of any other conveyance has priority over a deed for the same property that was delivered by the same seller but not recorded before the one that was recorded. CC §§1107, 1214. Once properly recorded, a buyer's deed provides constructive notice to all persons, whether they look at the record or not, and has priority over any other transfer. See CC §1214; *Triple A Mgmt. Co. v Frisone* (1999) 69 CA4th 520, 81 CR2d 669. By contrast, if a buyer fails to record the deed, subsequent bona fide purchasers or encumbrancers who record first will gain priority over the prior unrecorded deed. *Wilson v Nichols* (1940) 39 CA2d 527, 103 P2d 1007.

© The Regents of the University of California

§15.87 C. Defects or Exceptions to Constructive Notice

Not every document recorded provides constructive notice. Surveys do not impart constructive notice, because a record of survey is not an instrument or a conveyance under CC §§1213, 1215. *Stearns v Title Ins. & Trust Co*. (1971) 18 CA3d 162, 95 CR 682. Similarly, recorded notices of default or notices of sale relating to nonjudicial foreclosures do not provide constructive notice. CC §2924b(f); *Glavinich v Commonwealth Land Title Ins. Co.* (1984) 163 CA3d 263, 209 CR 266.

Certain defects in a recorded document may preclude that document from providing constructive notice. For example, a deed that incorrectly describes the land it is intended to convey does not give constructive notice of the transfer of that land (*Davis v Ward* (1895) 109 C 186, 41 P 1010), nor would recording a forged instrument give constructive notice of its existence (*Hopkins v Fresno County Abstract Co*. (1918) 36 CA 699, 173 P 106). With respect to defects in the execution of an instrument, or in the certificate of acknowledgment or lack of a certificate, CC §1207 provides generally that, if otherwise properly recorded, such instruments give constructive notice 1 year after recordation, despite the defect.

Not all defects are caused by the parties. The county recorder may improperly index an instrument, with the result that the instrument provides no constructive notice. See *Hochstein v Romero* (1990) 219 CA3d 447, 268 CR 202. The recorder may be held liable for damages if the recorder acts willfully or negligently in recording or indexing a document. Govt C §§27203-27203.5.

© The Regents of the University of California

D. Procedures for Recording

§15.88 1. Form of Instrument

Government Code §27361.6 requires a special format for documents to be recorded. The top 2½ inches of the first page is reserved for recording information. The left 3½ inches of that space is reserved for the name and address of the person requesting recordation and return of the document. (When the document is a deed conveying fee title, the name and address of the person to whom future tax statements are to be mailed must be stated in the left 3½ inches as well, although lack of this statement does not affect constructive notice. Govt C §27321.5.) The entire document must have ½-inch margins on each vertical side. Govt C §27361.6. See also §§10.8-10.12 on recording deeds.

The county recorder copies the original recorded documents and will, therefore, refuse to record illegible documents. Documents must be prepared on a quality of paper that will reproduce legibly. Common reasons that documents are rejected include small font size, already copied legal descriptions, blurred notary seal imprints, and site plans with cross-hatching or overlapping words and lines. Govt C §27361.6.

NOTE: Experimental programs are underway to test recording of digital images. Qualifying title insurers, licensed underwritten title companies, and specified state and federal governmental entities may record digitized images of a recordable instrument in lieu of a written paper document in the counties of Orange and San Bernardino. Effective January 1, 2000, other persons approved by the country recorders of those counties may also record digitized images. Govt C §§27279.1, 27279.3.

The content of a document must be written in English unless a certified translation is attached. Govt C §27293. The real property affected must be sufficiently described, either by a legal description in the document or by reference to another recorded document that contains such a description. If an instrument affects two parcels of real property, such as a deed granting an easement, both the benefited and burdened parcels must be described. CC §1468.

Government Code §27288.1 requires that the names of the owners of interests being transferred be the same as the names the owners used when the interests were acquired.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.89 2. Acknowledgments

§15.89 2. Acknowledgments

The recording statutes require that most documents to be recorded must contain an acknowledgment of the signature (Govt C §27287; see also CC §1188) of each person or persons whose real property is affected or alienated (Govt C §27288), *i.e.,* each grantor, lessor, or mortgagor, but not a grantee, lessee, or mortgagee. The acknowledgment is a statement that the person purporting to have signed the document did in fact sign it. See CC §1185 for the requirements of acknowledgments, and see CC §1189 for a statutory form. Documents that are not "instruments" need not be acknowledged to be recorded. *U.S. Hertz, Inc. v Niobrara Farms* (1974) 41 CA3d 68, 116 CR 44 (notice of default under deed of trust not an "instrument").

Normally, acknowledgments are prepared by a notary public. See CC §1181. The notary may acknowledge the signature of an individual who provides the notary with satisfactory evidence that the person making the acknowledgment is the individual who is described in and who executed the instrument. CC §1185(a). The definition of "satisfactory evidence" includes not only the oath or affirmation of a credible witness personally known to the acknowledging officer or two credible witnesses whose identities are proven to the officer by "satisfactory evidence," but also certain documentary evidence, such as a California identification card or driver's license or a passport. CC §1185(b)(3). As of January 1, 2008, notaries may no longer use "personal knowledge" to establish identity.

PRACTICE TIP: The California Legislature amended laws relating to notaries and notarization of documents, which take effect January 1, 2008. One change, which affects everyone who uses a notary or seeks to record a document with a recorder's office in California, alters the required wording of the statutory form of acknowledgement. County recorders are likely to reject any document submitted for recording that does not contain the new wording. See CC §1189.

There is no constructive notice of the transfer of an interest of nonacknowledging parties. *DuRoss v Trainor* (1932) 122 CA 732, 10 P2d 763. However, lack of an acknowledgment required for recording purposes does not alter the enforceability of the document between the parties or against one having actual knowledge of its contents. *Johndrow v Thomas* (1947) 31 C2d 202, 187 P2d 681. Some documents, such as homestead declarations (CCP §§704.910-704.995), must be acknowledged to be valid. See CCP §704.930(b). Under CC §1207, a recorded instrument, otherwise valid, imparts constructive notice 1 year after it has been recorded, regardless of any defect in the acknowledgment.

A statutory form (CC §1189) or a substantially similar form of certificate of acknowledgment must be endorsed on or attached to the instrument. CC §1188. A certificate of acknowledgment taken in another place is sufficient in California if it is taken in accordance with the laws of the place where the acknowledgment is made. CC §1189(b).

PRACTICE TIP: Care must be taken to distinguish between an acknowledgment that complies with CC §1189 and a so-called witness acknowledgment that complies with CC §1195. The witness acknowledgment acknowledges the signature of a witness who observed the signing of the instrument, in which case both the signer and the witness must sign the instrument. A witness acknowledgment is not sufficient to prove the execution of a grant deed, mortgage, deed of trust, quitclaim deed, or security agreement. CC §1195(b).

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.90 3. Place of Recording

§15.90 3. Place of Recording

Instruments or conveyances are recorded in the office of the county recorder in which the land is located. Govt C §24250.

To impart constructive notice, the instrument or conveyance must be recorded in the county (or counties, if the land is located in more than one) where the affected real property is situated. A certified copy of the recorded document can be recorded in any other counties in which affected property is located. CC §1213.

When the land is located in multiple counties, there is authority for the proposition that recording a document in one county will give constructive notice effective in the county of recordation regardless of the failure to record in other counties where the land is also situated. *Votypka v Valentine* (1919) 41 CA 74, 182 P 76.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.91 4. Recorder's Procedure

§15.91 4. Recorder's Procedure

The county recorder collects statutory fees before a document may be recorded. Govt C §27361. County recorders also collect other fees, such as the documentary transfer tax, before recordation. See §10.11 on documentary transfer tax requirements. Certain instruments are exempt from the documentary transfer tax. Rev & T C §§11921-11930.

The county recorder's most important task is organizing each recorded document—called indexing—so that it may be found in a search of the official records. Although recorded documents usually contain a legal description of the property affected, the recorder indexes documents according to the names of the parties affected. The names are indexed and compiled into two lists: the grantor index includes the names of parties conveying, transferring, assigning, or suffering (in the case of an abstract of judgment) an interest in the property, and the grantee index includes the names of parties acquiring or claiming an interest. Because of the complexity of legal descriptions, any index of the property based on legal descriptions would be significantly less accessible than one based on names.

Thousands of instruments are recorded daily in California, so proper indexing is obviously crucial to finding a particular document. Accordingly, California courts have held that the conclusive imputation of constructive notice of the contents of a recorded instrument is only fairly applied when the instrument may actually be located by a search of the proper indexes. *Hochstein v Romero* (1990) 219 CA3d 447, 268 CR 202.

The grantor/grantee indexes provide constructive notice of documents recorded within the chain of title. For example, a party may record a document too soon. If a deed of trust is recorded before the trustor records its grant deed (as owner), the deed of trust will be outside the chain of title and provide no constructive notice. It would be a "wild" document. *Far W. Sav. & Loan Ass'n v McLaughlin* (1988) 201 CA3d 67, 246 CR 872. Of course, the deed of trust would still be valid between the parties to the document. For further discussion of wild documents, see California Title Insurance Practice, chap 4 (2d ed Cal CEB 1997).

PRACTICE TIP: Title companies do not search by the grantor/grantee index method. Rather, electronic searches are performed that retrieve documents posted to the property, usually according to assessor's parcel numbers. Thus, a wild document under the grantor/grantee system may be found and included in a preliminary report issued by the title company. Once observed, the wild document provides actual notice of it, even though it might not have provided constructive notice because of improper indexing or a defect in the document. Also, a deed of trust recorded without a legal description may be posted to the property by a street address or assessor's parcel number referenced within the deed of trust. Although arguably a defective document, its inclusion as an exception in a preliminary report would provide actual notice of its existence to those who read the preliminary report.

© The Regents of the University of California

§15.92 5. Timing of Recording

The time at which a document is deemed "recorded" differs for constructive notice purposes and the legal effectiveness of the document. An instrument is considered "recorded" when it is deposited for recordation in the recorder's office with the proper officer. CC §1170. A recorded document provides constructive notice of the conveyance "from the time it is filed with the recorder for record." CC §1213. Nevertheless, courts have held that a document must be physically copied in the proper book and indexed before it is "recorded" and therefore provides constructive notice. See *Dougery v Bettencourt* (1931) 214 C 455, 6 P2d 499; *Cady v Purser* (1901) 131 C 552, 63 P 844. On constructive notice, see §§15.86-15.87.

By contrast, recording that is intended to comply with a statutory requirement or that is an essential step in completing some act of the party constitutes a recording as of the date the instrument is filed. See *Dougery v Bettencourt, supra; Cady v Purser, supra.*

Because the recorder has been interpreted to be the agent of a grantee or mortgagee (see 13 Ops Cal Atty Gen 185, 187 (1949)), such a grantee or mortgagee has a duty to verify that the instrument which reflects the information intended to be recorded is properly recorded.

In one case, a court ordered the retroactive recordation of a claim of lien when a county recorder delayed recording a submitted document by improperly demanding additional fees before recording the document. *Carpenters Health & Welfare Trust Fund v Shafer* (1983) 146 CA3d 504, 194 CR 266. If the recordation had not been made retroactive to the date the document was submitted, which was the last day to timely file it, the claimant would have lost the right to foreclose on its claim of lien.

© The Regents of the University of California

§15.93 E. Processing Documents; Disbursing Funds

Another important function of the escrow holder is to process and distribute documents submitted by the parties. As discussed in §15.27, the documents continue to belong to the party who deposited them until the time of closing. The escrow holder often receives complicated instructions about assembling and handling documents. In many transactions, the escrow holder is also asked to obtain signatures on the documents. Because of the contemplated title insurance policy, the escrow holder may insist on witnessing and acknowledging the signatures. All of these functions require that the parties deposit documents into escrow well before the expected closing date. Again because of the contemplated title insurance policy, the escrow holder may have to transfer documents to a title department or title insurer for review and handling before closing. After such review, the title insurer may require additional time to submit the documents to the county recorder for advance approval. If at any point the documents must be revised, the parties will need time to accomplish the revisions and obtain another round of approvals.

The escrow holder will use the funds on deposit to discharge liens, pay demands submitted, and pay the costs of escrow and title fees. This function is governed by the instructions of the parties and their title requirements. See §§4.134-4.135; for forms, see §§15.58, 15.69. If a party instructs the escrow holder to disburse funds to a nonparty on the basis of an assignment of that party's proceeds, and the escrow holder has knowledge of the assignment, the escrow holder will be liable to the nonparty for failure to follow the instructions in accordance with the assignment, even if the party attempts to cancel the instruction to pay. *Builders' Control Serv. v North Am. Title Guar. Co.* (1962) 205 CA2d 68, 22 CR 712.

Payoff demand statements received by the escrow holder will be paid and liens discharged in accordance with the parties' instructions.

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/15 Escrow and Closing the Sale/§15.94 F. Real Estate Commission

§15.94 F. Real Estate Commission

Real estate commissions are generally paid through escrow, but the escrow holder can only pay them to a broker. See Bus & P C §10138. The broker will then pay directly any agent that is involved.

Brokers often put irrevocable assignment language into their contracts to prevent the sellers from unilaterally instructing the escrow holder to pay lower commissions or no commissions at all. By adding the irrevocable assignment language, brokers are assured that they are parties to the escrow for the purpose of receiving their commission. *Builders' Control Serv. v North Am. Title Guar. Co.* (1962) 205 CA2d 68, 22 CR 712.

EXAMPLE: The California Association of Realtors® contract states that "Brokers are a party to the escrow for the sole purpose of compensation.... Buyer and Seller irrevocably assign to Brokers compensation specified in paragraphs..., respectively, and irrevocably instruct Escrow Holder to disburse those funds to Brokers at Close of Escrow...." Other real estate contracts contain language that is substantially similar. See §6.24.

Without further authorization from a party to the escrow, the brokers cannot cancel an escrow and the broker cannot amend an instruction unrelated to fees. A broker can only amend an instruction related to fees. The amendment must be approved by the other party to the escrow who has an interest in the broker fees: the seller. If the seller does not agree with the broker's amendment, the escrow holder is faced with conflicting instructions from two parties to the escrow.

If a seller instructs the escrow holder not to pay commissions or to pay reduced commissions when the purchase agreement contains irrevocable assignment language, a conflict exists between two parties to the escrow: the seller and the broker. The escrow holder cannot take sides when there is a conflict between any of the parties to the escrow, and must remain neutral. When a seller instructs the escrow holder not to pay a broker, the escrow holder should hold the funds pending mutual instructions from the parties (broker and seller) or a final court order regarding the funds. The escrow holder can also safely interplead the funds. On interpleader, see §15.98.

© The Regents of the University of California

§15.95 G. Real Estate Settlement Procedures Act (RESPA)

The Real Estate Settlement Procedures Act (RESPA) (12 USC §§2601-2617) was enacted in 1974 to ensure that borrowers receive adequate and timely information on the costs of obtaining a loan. Its additional purpose is to protect borrowers from unnecessarily high costs associated with borrowing funds to purchase a home. 12 USC §2601. The goal of RESPA is to have effective advance disclosure of settlement costs (12 USC §2601(b)(1)), eliminate kickbacks or referral fees (12 USC §2607(b)(2)), reduce the amount that borrowers are required to place in a lender's escrow account to pay for real estate taxes and insurance (12 USC §2601(b)(3)), and prohibit the seller from forcing the buyer to use a specific title insurance company (12 USC §2608).

RESPA applies to federally related mortgage loans, which are those typically used to finance the purchase of a one-to-four-family structure. 12 USC §2602(1)(A). Business, commercial, and agricultural loans are not subject to RESPA requirements. 12 USC §2606(a)(1). In practice, however, the escrow holder generally provides the same forms in all transactions, including those exempt from RESPA, to provide a consistent and familiar manner of designating the debits and credits in the transaction.

RESPA requires the lender to provide the borrower with an estimated settlement statement, before the close of escrow to review at least 1 day before the closing. At closing, the escrow holder prepares a HUD-1 Uniform Settlement Statement and delivers it to the borrowers after closing. 12 USC §2603. The Department of Housing and Urban Development (HUD) recently amended the RESPA regulations (Regulation X), 24 CFR §§3500.1-3500.23. The amendments clarify the contents of the basic disclosure forms provided to the borrower and establish specific tolerances for increases in the loan costs that may occur between estimation and closing.

The Good Faith Estimate (GFE) (24 CFR §3500.7) provides a clear summary of loan terms and discloses specific estimates of the origination charges and the cost of settlement services for the borrower. A copy of the GFE is provided in App X. The basic terms of the loan (including amount, term, interest rate, prepayment penalty, balloon payment, negative amortization, and variable interest) are all set out. Any increase in the loan costs at closing must be within a specific tolerance. Under 24 CFR §§3500.7(e)-(f), the amount stated in the GFE for loan origination fees (when an interest rate is locked), credit charges, adjusted origination fees, and transfer taxes may not increase at closing.

Some costs are allowed to increase but, by no more than 10 percent. *i.e.,* lender required settlement services (if the lender selected the provider), title insurance (if the lender selected the provider), and recording fees. For the costs that are allowed to increase by 10 percent, settlement service providers are allowed to use average costs for services that are not based on the value of the property or the loan, *e.g.,* credit reports and courier fees. 24 CFR §§3500.8. If the lender can show that circumstances have changed, the GFE may be revised. If there are violations, the loan originator may cure by reimbursing the borrower within 30 days. 24 CFR §3500.7(i).

The new HUD-1 Settlement Statement form was designed to allow borrowers to easily connect the costs found on the GFE to the charges on the HUD-1 Settlement Statement. For a cost included on the GFE, the HUD-1 Settlement Statement specifically directs the borrower to the lines in the GFE that match the associated cost. A copy of the HUD-1 Settlement Statement is reproduced in App Y. The new forms must be used beginning January 1, 2010.

RESPA also requires the lender to provide the borrower with informational booklets regarding the fees to be charged. The specifics of what the booklet must include are set forth in 12 USC §2604. Lenders are not permitted to charge their borrowers for preparation of the truth-in-lending booklets, Uniform Settlement Statements, or escrow account statements. 12 USC §2610.

© The Regents of the University of California

§15.96 H. Holdbacks

Sometimes parties to an escrow have issues that remain unresolved at closing. Frequently termite work, minor repairs, or leasebacks create situations that make the parties want the escrow holder to hold funds. The escrow holder may have to hold funds when there is a dispute among parties to the escrow regarding disbursal of proceeds. This frequently arises when there is a dispute regarding real estate commissions.

When there is a dispute about disbursement of funds, the parties may want the escrow holder to hold the funds until the dispute is resolved. Any holdback situation can result in protracted litigation or a hold of funds for an extended period of time. If there is a holdback, the parties have a common goal—to reach an agreement that will allow the escrow holder to pay the funds in a short period of time. For a form of supplemental escrow instructions for funds held, see App Z.

Instead of the escrow holder, the parties may select an arbitrator or mediator to hold the funds. Alternatively, some parties agree to deposit the funds in a joint bank account requiring both signatures for withdrawal. The funds may also go into an attorney's trust account in accordance with an agreement with the parties. The escrow holder will follow mutual instructions from the parties on where to deposit the funds. However, often the parties who are already in a dispute may not agree on escrow instructions regarding the funds. The escrow holder will then interplead the funds. See §15.98.

© The Regents of the University of California

XII. FAILED TRANSACTIONS

§15.97 A. Cancellation of Escrow

When a transaction fails, the escrow holder will prepare cancellation instructions for the parties to sign that clearly state that the transaction is cancelled and provide for the return of the documents and deposits held by the escrow holder. Sometimes the cancellation instructions provide for the payment of various bills that the parties have incurred in connection with the contemplated transaction (*e.g.,* termite inspections, appraisal fees, escrow fees). For a form of cancellation instructions, see App AA.

For a form provision regarding the effect of cancellation on deposits, see the California Association of Realtors® Residential Purchase Agreement and Joint Escrow Instructions, ¶14.E, in §6.24. Sometimes the general provisions contain terms that can be used to resolve a dispute on cancellation. See, for example, paragraph 10 of the general provisions in App S.

PRACTICE TIP: An attorney preparing a purchase agreement should include a provision specifying what will happen on cancellation. See, for example, §4.177. A clearly drafted contract makes it easier to avoid unresolved conflicts that can result in litigation. Even the best drafting cannot, however, prevent subsequent conduct of the parties that can result in waiver of significant terms. See *Galdjie v Darwish* (2003) 113 CA4th 1331, 7 CR3d 178, discussed in §15.59. See also *Peak-Las Positas Partners v Bollag* (2009) 172 CA4th 101, 90 CR3d 775 (affirming judgment of specific performance extending escrow), discussed in §4.149.

When an escrow holder is faced with conflicting instructions or a lack of instructions regarding deposited funds, the escrow holder has the option of interpleading the funds with the court. See §15.98.

Under Fin C §17421.5, licensed escrow holders may charge a fee for administering an escrow that has been postponed for at least 2 months or cancelled if certain requirements are met.

PRACTICE TIP: In Northern California, escrow instructions are often not signed until 3 days prior to close of escrow. If there is a cancellation of an escrow prior to signing the instructions, the cancellation fee may be vulnerable to challenge by the parties. On the differences in Northern and Southern California escrow procedures, see §15.8.

© The Regents of the University of California

§15.98 B. Interpleader

There are times when the parties cannot reach an agreement to give the escrow holder a matching instruction to resolve a dispute regarding the disposition of funds and/or documents held in an escrow. If the parties cannot resolve their dispute, the escrow holder may file an interpleader. CCP §§386-386.6. The escrow holder's attorney will initiate a lawsuit by filing a complaint in interpleader and depositing the disputed funds and documents with the court.

After the escrow holder serves the interpleader complaint on the parties to the escrow who are disputing the disposition of funds and documents, the escrow holder brings a motion for an order to discharge the escrow holder from liability and to dismiss the escrow holder from the action. CCP §386.5. The escrow holder can be dismissed because the actual dispute is between the buyer and the seller (or other principals). As a neutral third party, the escrow holder is merely a stakeholder and has no interest in who succeeds in the action. By initiating the interpleader action and obtaining a discharge from further liability, the escrow holder avoids tort liability. *Cantu v Resolution Trust Corp.* (1992) 4 CA4th 857, 6 CR2d 151.

The escrow holder may recover its attorney fees and costs, which are deducted from the funds that have been interpled with the court. CCP §386.6. See, for example, paragraph 11 in App S.

© The Regents of the University of California

§15.99 XIII. PRELIMINARY CHANGE OF OWNERSHIP REPORT

In 1984 the legislature enacted change-in-ownership reporting to aid the assessor's office in expediting reassessment of real property. In every real estate transaction involving the change in ownership of real property, the buyers must complete and send to the county recorder's office a preliminary change of ownership report (PCOR). Rev & T C §480.3. The PCOR is sent to the recorder's office concurrently with the document that evidences the change in ownership, usually a deed. If the buyer does not send a completed PCOR to the county recorder's office, the buyer is charged an additional recording fee of $20. Rev & T C §480.3(b). The PCOR is set forth in Rev & T C §480.4 and is reprinted in App BB.

© The Regents of the University of California

Appendixes

Appendix A	Transfers Triggering Reappraisal
Appendix B	Buyer's Comprehensive Commercial Property Acquisition and Due Diligence Checklist
Appendix C	Checklist of Due Diligence Materials to Be Delivered by Seller to Buyer in Sale Involving Commercial Leases
Appendix D	Board Resolution (Authorizing Purchase)
Appendix E	Limited Liability Company Certificate (Authorizing Purchase)
Appendix F	Statement of Partnership Authority (Secretary of State Form GP-1)
Appendix G	Grant Deed
Appendix H	Bill of Sale
Appendix I	Assignment of Leases
Appendix J	Assignment of Intangibles
Appendix K	Estoppel Certificate From Tenants
Appendix L	Tenant Letter
Appendix M	Spousal Waiver
Appendix N	Alternate Natural Hazard Conditions Disclosure
Appendix O	Sample Tenancy-in-Common Agreement
Appendix P	Access License and Indemnity Agreement
Appendix Q	Hotel Purchase and Sale Agreement
Appendix R	Estoppel Certificate From Hotel Operator
Appendix S	Escrow Instructions—General Provisions
Appendix T	Real Estate Withholding—Computation of Estimated Gain or Loss (FTB Form 593-E)
Appendix U	Real Estate Withholding Certificate (FTB Form 593-C)
Appendix V	Real Estate Withholding Installment Sale Agreement (FTB Form 593-I)
Appendix W	FIRPTA Certification
Appendix X	Buyers/Borrowers Estimated Closing

	Statement
Appendix Y	Settlement Statement
Appendix Z	Supplemental Escrow Instructions—Funds Held
Appendix AA	Escrow Cancellation Instructions
Appendix BB	Preliminary Change of Ownership Report

© The Regents of the University of California

Appendix A

Transfers Triggering Reappraisal

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

Type of Transfer	Action Required	Remarks—Rev & T C and 18 Cal Code Regs
Condominiums and Cooperatives		
1. Transfer of a unit in a complex with common areas or facilities (housing cooperative, condominium, community apartment project, shopping center, *etc*.).	Reappraisal of the unit transferred and of appurtenant common area	Increased values are not to be prorated by the owner to the other units. Rev & T C §§61(i), 65.1; 18 Cal Code Regs §462.001.
2. Transfer of stock in a housing co-operative with possessory right in a specific unit.	Reappraisal	Reappraise the unit transferred and any common area appurtenant. Rev & T C §61(i); 18 Cal Code Regs §§462.001, 462.180(a). See Rev & T C §62(i) and 18 Cal Code Regs §462.180(b) for exceptions. Increased values are not to be prorated by the owner to the other units. Rev & T C §65.1.
Corporations		
3. Corporation *A* transfers property to unrelated Corporation *B*.	Reappraisal	Transfer is from one entity to another. Rev & T C §60. See Rev & T C §64 and 18 Cal Code Regs §462.180(a).
4. Transfers among affiliated groups (and nontaxable corporate reorganizations under IRC §368 among members of affiliated groups).	No Reappraisal	See definition of "affiliated." Rev & T C §64(b); 18 Cal Code Regs §462.180(b).
5. Person or "legal entity" obtains control of corporation.	Reappraisal	Control: Purchase sufficient stock to give more than 50% of voting stock. Rev & T C §64(c); 18 Cal Code Regs §462.180(d).
5.1. Purchase or transfer of stock—no control.	No Reappraisal	18 Cal Code Regs §462.180(c).
6. One corporation obtaining control of	No Reappraisal	See definition of "affiliated." Rev & T C §64(b); 18 Cal

affiliated corporation.		Code Regs §462.180(b).
Interspousal/Registered Domestic Partner		
7. Transfer of property between spouses or registered domestic partners.	No Reappraisal	Change in ownership shall not include any interspousal or registered domestic partner transfers (includes transfers between January 1, 2000, and January 1, 2006, and any reassessment must be reversed if application is made before June 30, 2009). Rev & T C §62; 18 Cal Code Regs §462.220.
8. Transfer between ex-spouses or ex-registered domestic partners in connection with a decree of dissolution of a marriage or partnership.	No Reappraisal	Excluded even though parties are ex-spouses or ex-registered domestic partners. Rev & T C §63(c); 18 Cal Code Regs §462.220(c).
9. Property is transferred to a trustee for the beneficial use of the spouse or registered domestic partner of the transferor	No Reappraisal	Excluded even though transfer is to a trustee and not spouse or registered domestic partner. Rev & T C §63(a); 18 Cal Code Regs §462.220(a).
Joint Tenancy		
10. *A* and *B* acquire property as joint tenants.	Reappraisal	Transfer of fee title. Rev & T C §§60, 61(e); 18 Cal Code Regs §§462.001, 462.040(a).[1]
11. Person *A* owning property in severalty adds person *B* as a joint tenant.	No Reappraisal	Person *A* is transferor and joint tenant after the creation of the joint tenancy. Rev & T C §§62(f), 65(b); 18 Cal Code Regs §462.040(b).
a. *A* transfers his interest to *C* (*B* and *C* become tenants in common.)	Reappraise 100%	Termination of an original transferor's[1] interest in a joint tenancy may be excluded under Rev & T C §65(c); 18 Cal Code Regs §462.040(b). Held by original transferor[1] before creation of joint tenancy. Rev & T C §65.
b. *B* transfers his interest back to *A*. (Ignore a, above.)	No Reappraisal	Termination of an interest of other than an original transferor[1] in a joint tenancy excluded under Rev & T C §62(f); 18 Cal Code Regs §462.040(b)(3). The interest reverts to an original transferor,[1] so reappraisal not warranted. Rev & T C §65(b);

		18 Cal Code Regs §462.040(b)(2).
12. *A* and *B* own property as joint tenants. They purchased it together from another individual. *B* dies.	Reappraisal of the interest transferred 50%	Termination of a joint tenancy interest. Rev & T C §§61(e), 65(a), 65.1; 18 Cal Code Regs §§462.001, 462.040(a). 18 Cal Code Regs §462.040(b) has no bearing because the joint tenancy is not one excluded from reappraisal under Rev & T C §62(f).
13. *A* and *B* as joint tenants sell to *H* and *W* (husband and wife) as joint tenants	Reappraisal	Not solely between spouses. Rev & T C §§60, 61(e).
a. *H* dies.	No Reappraisal	Interspousal exclusion. Rev & T C §§63(b); 18 Cal Code Regs §462.040(b)(5).
14. *H* and *W* own property as joint tenants and grant to *H*, *W*, *S*, and *D* as joint tenants.	No Reappraisal	*H* and *W* are transferors and joint tenants. Rev & T C §62(f); 18 Cal Code Regs §462.040(b)(1).
a. *H* dies.	No Reappraisal	*W* still an original transferor.[1]
b. *W* dies—property goes to *S* and *D*.	Reappraisal	100%—termination of original transferor's interest. Rev & T C §65(c).
c. *S* and *D* grant back to *H* and *W* (ignore a. and b. above).	No Reappraisal	Property reverts to original transferors. Rev & T C §65(d); 18 Cal Code Regs §462.040(b)(3).
15. *A* and *B* own property as joint tenants and grant to *A*, *B*, *C*, and *D* all as joint tenants.	No Reappraisal	*A* and *B* are transferors and joint tenants after transfer. Rev & T C §62(f); 18 Cal Code Regs §462.040(b)(1).
a. *A* dies.	No Reappraisal	Vests by operation of law in *B*, who is original transferor and still joint tenant. Rev & T C §65(c); 18 Cal Code Regs §462.040(b).
b. *A*, *B*, *C*, and *D* grant to *B*, *C*, and *D* (ignore a. above).	No Reappraisal	An original transferor still holds an interest. Rev & T C §65(c); 18 Cal Code Regs §462.040(b)(2).
c. *B*, *C*, and *D* grant to *B* (after either a. or b.).	No Reappraisal	The interest of *C* and *D* were other than original transferor's interests and reverted to original transferor *B*. Rev & T C §65(d); 18 Cal Code Regs §462.040(b)(2).
16. *A* grants property to *A* and *B* as joint	No Reappraisal	*A* is transferor and joint tenant after transfer. Rev & T C

tenants.		§62(f); 18 Cal Code Regs §462.040(b)(1).
a. Subsequent to transfer in 16, *A* and *B*, as joint tenants, grant *A* and *B* as equal tenants in common.	Reappraisal	Reappraisal of *B*'s (*B* is not original transferor). Rev & T C §§65; 18 Cal Code Regs §462.020(a).
b. *A* and *B* (both original transferors) joint tenants grant *A* and *B* as equal tenants in common.	No Reappraisal	*A* and *B* were and are equal co-owners. Rev & T C §§62(a), 65(c); 18 Cal Code Regs §§462.020(b), 462.040(b)(4)(B).
Leases[2]		
17. Creation of a leasehold interest in taxable real property for a term of 35 years or more.	Reappraisal	Reappraisal of full fee (leasehold and leased fee); term includes renewal option. Rev & T C §61(c); 18 Cal Code Regs §§462.100(a)(1)(A), 462.100(d).
18. Leasehold interest that had an *original* term of 35 years or more transfers or reverts to lessor.	Reappraisal	Reappraisal of fee; term includes renewal options. Rev & T C §61(c); 18 Cal Code Regs §§462.100(a)(1)(C), 462.100(d).
19. Transfer of a lessee's leasehold interest with a *remaining* term of 35 years or more.	Reappraisal	Reappraisal of fee; term includes renewal options. Rev & T C §61(c); 18 Cal Code Regs §§462.100(a)(1)(B), 462.100(d).
20. Transfer (other than by termination) of a lessee's leasehold interest with a *remaining* term of less than 35 years.	No Reappraisal	Term includes renewal options. Rev & T C §61(c); 18 Cal Code Regs §§462.100(b)(1)(B), 462.100(d).
21. Transfer of a lessor's interest in real property subject to a lease with a *remaining* term of less than 35 years.	Reappraisal	Reappraisal of fee; term includes renewal options. Rev & T C §61(c); 18 Cal Code Regs §§462.100(a)(2)(A), 462.100(d).
22. Transfer of a lessor's interest in real property subject to a lease with a *remaining* term of 35 years or more.	No Reappraisal	Includes transfer to lessee; term includes renewal options. Rev & T C §62(g); 18 Cal Code Regs §§462.100(b)(2)(A), 462.100(d).
Life Estates		
23. Person *A* grants title to person *B*, reserving a life estate.	No Reappraisal	*A* retains present interest and beneficial use. Rev & T C §62(e); 18 Cal Code Regs §462.060(a).

a. *A* dies.	Reappraisal	Right of possession vests in *B*. Rev & T C §§61(g), 62(e); 18 Cal Code Regs §462.060(a). Except when *B* is spouse of *A*. Rev & T C §63(b); 18 Cal Code Regs §§462.060(a), 462.220(b).
24. Person *A* grants title to person *B* for life with remainder to *C*.	Reappraisal when life estate granted	Transfer of present interest and beneficial use. Rev & T C §60; 18 Cal Code Regs §462.060(a). Except if *B* is spouse of *A*. Rev & T C §63; 18 Cal Code Regs §462.220.
a. *B* dies—*C* takes property.	Reappraisal	Termination of precedent interest. Rev & T C §62(e); 18 Cal Code Regs §462.060(a). Right to possession vests in *C*. Rev & T C §60. Except if *C* is spouse of *B*. Rev & T C §63(b); 18 Cal Code Regs §§462.060(a), 462.220(b).
Mineral Rights		
25. Creation, renewal, sublease, assignment, or other transfer of right to produce or extract oil, gas, or other minerals.	Reappraisal of the right transferred	Property other than mineral rights not reappraised. Rev & T C §61(a); 18 Cal Code Regs §§468-469.
Mobilehome Park		
25.1 Transfer of mobilehome park to certain entities formed by tenants to purchase park.	No Reappraisal	Rev & T C §§62.1-62.2.
Partnerships		
26. Transfer of real property from a partnership to a partner.	Reappraisal	Rev & T C §61(j); 18 Cal Code Regs §462.180(e)(1). Rev & T C §62(a)(2) and 18 Cal Code Regs §462.180(b)(2) do not apply when there is a change in proportional interests in real property.
27. Transfer of real property from a partnership of *A* and *B* to *A* and *B* as tenants in common.	No Reappraisal	Rev & T C §62(a)(2); 18 Cal Code Regs §§462.020(b), 462.180(b)(2). If solely a change in method of holding title, resulting in interests in property being held in same proportion.
28. *A* and *B* are partners in the *A* and *B* partnership *which is a continuing partnership*. *C* is added as a partner.	No Reappraisal	Rev & T C §64(a); 18 Cal Code Regs §462.180(e)(2).

29. Changing the name of the *A* and *B* partnership above to the *A, B, C,* partnership.	No Reappraisal	18 Cal Code Regs §462.001.
30. [Reserved]		
Possessory Interest		
31. Creation, renewal, extension, sublease, or assignment of a taxable possessory interest in tax-exempt real property.	Reappraisal	Ownership change does not result from any renewal or extension during the reasonably anticipated term of possession used by the assessor to value the interest or with respect to a sublease for less than half the length of the remaining term of the leasehold, including renewal options. Rev & T C §§61(b), 62(o); 18 Cal Code Regs §462.080. Renewal or extension during term used by accessor does not cause reappraisal until renewal or extension period begins. 18 Cal Code Regs §462.080(b)(2).
Tenancy in Common		
32. Two or more people acquire property as tenants in common.	Reappraisal	Transfer is of fee title. Rev & T C §§60, 61(f); 18 Cal Code Regs §462.020.
33. A person holding title as a tenant in common transfers his or her interest to one of the other tenants in common.	Reappraisal of the interest transferred	Rev & T C §61(f); 18 Cal Code Regs §462.020(a). Except when interspousal exclusion applies or when interest transferred is less than 5% and less than $10,000. Rev & T C §§61(f), 63, 65.1; 18 Cal Code Regs §§462.020(b)(2)-(3), 462.220.
34. *A, B, C,* and *D* hold title as tenants in common with 25% interest each. *D* sells his interest to *T*.	Reappraisal of the interest transferred	*T* now has an undivided ¼ interest in common with *A, B,* and *C*. Rev & T C §§61(f), 65.1; 18 Cal Code Regs §462.020.
Transfer of Fee Title Generally		
35. Transfer of fee title to land and/or improvements from one person to another.	Reappraisal of the interest transferred	Rev & T C §60; 18 Cal Code Regs §462.001. Except as otherwise excluded in this table or if a total of less than 5% and less than $10,000 undivided interest transfers during an assessment year. Rev & T C §65.1; 18 Cal Code Regs §§462.020(b)(2),

		462.040(b)(6).
35.1. Transfer of fee title to certain disabled children and wards.	No Reappraisal	Rev & T C §62(n). Applies only if disabled for at least five years previously; property was principal residence for five years previously; adjusted gross income of child or ward and parents and spouse is no more than $20,000. (For definition of principal residence, see Rev & T C §63.1.)
Trust:		
Irrevocable Trusts		
36. Transfer of property from *A* to *C* as trustee naming persons *A* and *B* as beneficiaries.	Reappraisal to the extent *B* is a beneficiary	Rev & T C §62(d)(1); 18 Cal Code Regs §462.160(b)(1). Reappraise per Rev & T C §61(h) and 18 Cal Code Regs §§462.160(c)-(d).
37. Transfer of property from person *A* to trust for the benefit of person *B* for a term of 12 years; reversion to *A*.	No reappraisal at creation or termination	The beneficial interest of other must *exceed* 12 years to be a change in ownership. Rev & T C §62(d); 18 Cal Code Regs §462.160(d)(3).
38. Transfer of property from *A* to *C* as trustee, naming person *B* as the sole beneficiary.	Reappraisal of the interest transferred to *B*	Rev & T C §§60, 61(h); 18 Cal Code Regs §462.160(a). Except when *B* is spouse of *A*. Rev & T C §63(a); 18 Cal Code Regs §§462.160(b)(3), 462.160(d)(4), 462.220(a).
39. Person *A* as beneficiary of a trust owning real property assigns his or her beneficial interest to person *B*.	Reappraisal if a present beneficial interest transfers	Rev & T C §60; 18 Cal Code Regs §462.001. Except when beneficial interest does not exceed 12 years and property reverts to trustor or when *B* is spouse of *A*. Rev & T C §§62(d), 63; 18 Cal Code Regs §462.160(b)(3), 462.220.
	No reappraisal if a future beneficial interest transfers	Rev & T C §60; 18 Cal Code Regs §462.001. Reappraise when *B* receives a present interest, unless interspousal. Rev & T C §63; 18 Cal Code Regs §462.220.
40. Transfer of property from person *A* to person *A* as trustee naming person *A* as the sole beneficiary.	No Reappraisal	There is no transfer of a present interest or beneficial use. This does not qualify as a trust under California law. Rev & T C §60; 18 Cal Code Regs §462.001.
41. Transfer of property from person *A* to person *B*, as trustee, naming persons *A* and	Reappraisal to the extent that *C* and *D* are present	*A* is not the sole beneficiary of the trust. Rev & T C §62(d)(1); 18 Cal Code Regs §462.160(b)(1). No reappraisal

C as income beneficiaries; remainder to *D*.	beneficiaries	to the extent *C* or *D* is *A*'s spouse. Rev & T C §63; 18 Cal Code Regs §§462.160(b)(3), 462.220(a).
a. *A* dies.	Reappraisal of *A*'s interest	Rev & T C §61(g); 18 Cal Code Regs §462.160(c). Except if *A*'s interest passes to *A*'s spouse. Rev & T C §63(b); 18 Cal Code Regs §462.220(e).
b. *A* and *C* die—property to *D*.	Reappraisal	Rev & T C §61(g); 18 Cal Code Regs §462.160(c).Except if *D* is *A*'s spouse. Rev & T C §63; 18 Cal Code Regs §§462.160(b)(3), 462.220.
42. Transfer of property from *A* and *B* as joint tenants to *A* and *B* as trustees and life beneficiaries of the property; remainder to *C*.	No Reappraisal	No transfer of a present interest or beneficial use. Rev & T C §62(d)(1); 18 Cal Code Regs §462.160(b)(1).
a. *A* and *B* die.	Reappraisal	Termination of precedent interest. Right of possession vests in *C*. Rev & T C §61(g); 18 Cal Code Regs §462.160(c).
Revocable Trusts		
43. Transfer of property to a revocable trust. (Transferor and trustor are same party.)	No Reappraisal	Rev & T C §62(d)(2); 18 Cal Code Regs §462.160(b)(2). No reappraisal until trust becomes irrevocable. Rev & T C §61(h); 18 Cal Code Regs §462.160(b)(2).
44. *H* and *W* execute a revocable trust, transfer property into it with *H* and *W* as trustees and life beneficiaries; remainder to *C*.		
a. Creation	No Reappraisal	No transfer of a present interest or beneficial use. Rev & T C §§60, 62(d); 18 Cal Code Regs §462.160(b)(2).
b. Revocation by *H* and *W*.	No Reappraisal	No transfer of a present interest or beneficial use (both still held by *H* and *W*). Rev & T C §§60, 62(d); 18 Cal Code Regs §462.160(d)(2).
c. *H* and *W* die—*C* takes property. (Ignore b. above.)	Reappraisal	Termination of precedent interest (*H* and *W*). Right of possession vests in *C*. Rev & T C §61(g); 18 Cal Code Regs

		§462.160(c).
d. *H* dies, *W* revokes trust. (Ignore b. and c. above.)	No Reappraisal	No present interest transferred. Rev & T C §62(d); 18 Cal Code Regs §462.160(d)(2).
e. *H* dies, *C* dies, with *W* as sole heir of both. (Ignore b., c., and d. above.)	No Reappraisal	*C* predeceases *W*, so present interest stays in *W* as life beneficiary. Rev & T C §60.
Other Transfers		
45. Any transfer to an existing assessee to perfect or clear title by deed.	No Reappraisal	No present interest transferred. Rev & T C §§60, 62(b); 18 Cal Code Regs §462.240(a)(1).
Any transfer to an existing assessee to correct or reform a deed.	No Reappraisal	Original relationship between grantor and grantee cannot change. Rev & T C §62(*l*).
46. Creation or termination of a security interest without right of possession (trust deed or mortgage).	No Reappraisal	Rev & T C §62(c)(1); 18 Cal Code Regs §462.240(a)(2).
47. Substitution of trustee under security or trust instrument.	No Reappraisal	Rev & T C §62(c)(2); 18 Cal Code Regs §462.240(b).
48. *A* and *B* are co-owners of a piece of property. The property is partitioned, and *A* and *B* then have equal-value parcels owned in severalty.	No Reappraisal	This is a change in the method of holding title with no change in proportional interests (based on value). Rev & T C §62(a); 18 Cal Code Regs §462.020(b)(1).
49. *A* and *B* are co-owners; property is partitioned unequally. (Value of *B*'s portion differs from value of *A*'s portion.)	Reappraisal of the interest transferred	*A* receives *B*'s 50% interest in one parcel, and *B* receives *A*'s 50% interest in the other parcel. Rev & T C §61(f). Rev & T C §62(a) and 18 Cal Code Regs §462.020(b)(1) do not apply to unequal partitions.
50. Title to a property transfers by foreclosure sale with no further right of redemption.	Reappraisal	Fee transfer. Rev & T C §§60, 67; 18 Cal Code Regs §462.120(a)-(b).
51. Sale at auction of tax-deeded property.	Reappraisal	Fee transfer. Rev & T C §§60, 67; 18 Cal Code Regs §462.140.
52. Change of name.	No Reappraisal	No interest transferred. 18 Cal Code Regs §462.001.
53. Transfer of bare legal title to person, corporation, or other	No Reappraisal	No transfer of equitable title. 18 Cal Code Regs §462.240(a).

legal entity.

54. *R* purchases freehold estate from *Y*.	Reappraisal	A purchase is an ownership change. Rev & T C §§60, 65.1, 67; 18 Cal Code Regs §462.001.
55. Transfers to minor child or among minor siblings at death of parent.	No Reappraisal	No reappraisal if property transferred was minor's principal residence. Rev & T C §62(m).
56. Transfers between parents and children of the principal residence of either.	No Reappraisal	Rev & T C §63.1(a)(1).
57. Transfers between parents and children of real property other than personal residence.	No Reappraisal	No reappraisal of first $1,000,000 of full cash value per transferor. Rev & T C §63.1(a)(2), (b)(2).
58. Transfers between grand-parents and grandchildren of property described in paragraphs 56 and 57 above	No Reappraisal	For transfers on or after March 27, 1996, if both of the parents of that grandchild or grandchildren, who qualify as the children of the grandparents, are deceased as of the date of the purchase or transfer. (Stepparents need not be deceased.) Exemption applies only to first personal residence transferred and first $1,000,000 of other property transferred. Rev & T C §63.1(a)(3).
59. Reorganization of farm credit institutions under federal Farm Credit Act of 1971.	No Reappraisal	Rev & T C §64(b).

---

[1] Spouses of original transferors are considered original transferors for purposes of Rev & T C §65(f). There is a rebuttable presumption that a joint tenant before March 2, 1975, is an original transferor. See Rev & T C §65(e). See Rev & T C §65 for further provisions concerning original transferors.

[2] Homes on leased land that are eligible for homeowner's exemption are conclusively presumed to have a renewal option for at least 35 years. Rev & T C §62(g).

© The Regents of the University of California

Appendix B

Buyer's Comprehensive Commercial Property Acquisition and Due Diligence Checklist

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

This is a comprehensive checklist containing items beyond the normal scope of the attorney's duty. Some of the items will be undertaken by the client or a third-party professional (*e.g.,* accountant or engineer). some items will be required in some transactions (*e.g.,* acquisition of property to be developed, acquisition of tenanted property) but not in others. It is important for the attorney and the client to allocate responsibility among the various parties. Further, the scope of the attorney's due diligence obligations for each transaction should be specifically described in the attorney's retainer agreement. The attorney may wish to share this checklist with the client and to customize it for each transaction. For discussion of buyer's due diligence, see §§1.70-1.93. On seller's due diligence, see §§1.58-1.69.

Buyer's Comprehensive Commercial Property Acquisition and Due Diligence Checklist

I. SUMMARY

A. Property Location:_____

B. Seller Name:_____

C. Purchase Price:_____

D. Contingency Periods and Critical Dates

1. Title Contingency:_____
2. Inspection Contingency:_____
3. Environmental Contingency:_____
4. Financing Contingency:_____
5. Lease Review Contingency:_____
6. Other Contingencies:_____
7. Increase Deposit on:_____
8. Closing Date:_____

Item	*Party Responsible*	*Date Due*	*Date Done*

II. NEGOTIATION OF PURCHASE AGREEMENT
(see discussion in §§1.114-1.130)

A. Determine Form of Transaction
(see §§1.26-1.36; 1.94-1.103):

1. Straight Purchase	_____	_____	_____
2. Option (see chap 8)	_____	_____	_____
3. Ground Lease	_____	_____	_____
4. Sale and Leaseback	_____	_____	_____
5. Installment Sale	_____	_____	_____
6. Master Lease	_____	_____	_____

B. Draft and Negotiate Letter of Intent (see form in chap 3)	_____	_____	_____
C. Determine Purchasing Entity	_____	_____	_____
D. Determine Form of Purchase Agreement to Use	_____	_____	_____
E. Retain Attorneys To Handle Drafting and Negotiations			
1. Specify Attorney	_____	_____	_____
2. Discuss Fee Structure	_____	_____	_____
F. Negotiate Critical Terms of Agreement (see forms in chaps 4-6):			
1. Purchase Price	_____	_____	_____
2. Deposit	_____	_____	_____
a. Amount	_____	_____	_____
b. Timing	_____	_____	_____
c. Who holds	_____	_____	_____
d. Who receives interest	_____	_____	_____
e. Liquidated damages	_____	_____	_____
3. Specific Contingencies	_____	_____	_____
4. Contingency Periods	_____	_____	_____
5. Financing	_____	_____	_____
a. Third party	_____	_____	_____
b. Seller carry-back (see chap 9)	_____	_____	_____
c. Assumption of existing loans	_____	_____	_____
6. Extension Rights (Closing and Contingency)	_____	_____	_____
7. Closing Date	_____	_____	_____
8. Condition of Title (Survey)	_____	_____	_____
9. Title Company and Escrow	_____	_____	_____
10. Seller Covenants	_____	_____	_____
a. Rental guarantees	_____	_____	_____
b. Leasing activities pre-closing	_____	_____	_____
c. Completing current tenant improvements	_____	_____	_____
d. Pay unpaid leasing commissions	_____	_____	_____
e. Seller lease-back	_____	_____	_____
11. Representations and Warranties	_____	_____	_____
12. Indemnities	_____	_____	_____
13. Closing Costs and Commissions	_____	_____	_____
14. Proration Formulas	_____	_____	_____
15. Holdbacks for Repairs, Environmental, etc.	_____	_____	_____
G. Finalize Any Brokerage			

Arrangements	_____	_____	_____
H. Record Memorandum of Purchase Agreement	_____	_____	_____

III. CONTINGENCY PERIOD DUE DILIGENCE

A. Title and Escrow (on title, see §§1.33-1.39 and chap 4; California Title Insurance Practice (2d ed Cal CEB 1997); on escrow, see chap 15)			
1. Select Title Company (see Title Ins, chap 3)	_____	_____	_____
2. Order Preliminary Report and Copy of Exceptions (see Title Ins, chap 2)	_____	_____	_____
a. Specify ALTA or CLTA title policy (see Title Ins, chaps 6-8)	_____	_____	_____
b. Request survey update	_____	_____	_____
c. Get legible copies of exceptions	_____	_____	_____
d. Have all easements plotted	_____	_____	_____
e. Get copy of subdivision map	_____	_____	_____
f. Consider requesting chain of title	_____	_____	_____
g. Get current assessment amounts	_____	_____	_____
3. Order Survey (see chap 4)	_____	_____	_____
a. Select surveyor	_____	_____	_____
b. Negotiate cost	_____	_____	_____
c. Specify certification and scope	_____	_____	_____
4. Review Preliminary Report and Exceptions (see chap 4; Title Ins, chap 5)	_____	_____	_____
a. Liens	_____	_____	_____
b. Restrictions	_____	_____	_____
c. Taxes and assessments	_____	_____	_____
d. Easements	_____	_____	_____
e. Rights of Way	_____	_____	_____
f. Covenants, Conditions, and Restrictions (CC&Rs) and Reciprocal Easement Agreements (REAs) of record			
(1) Obtain estoppels	_____	_____	_____
(2) Review articles, by-laws and budgets of any association	_____	_____	_____
g. Property description	_____	_____	_____
(1) Are easements included?	_____	_____	_____
(2) Are REAs included?	_____	_____	_____
5. Determine If New Easements Needed	_____	_____	_____
6. Determine If New CC&Rs or REAs Needed	_____	_____	_____

7. Review Survey (see Title Ins, chap 4)	_____	_____	_____
a. Certification (to buyer and lender)	_____	_____	_____
b. Encroachments	_____	_____	_____
c. Easements	_____	_____	_____
d. Property description	_____	_____	_____
e. Deliver to title company	_____	_____	_____
8. Timely Object to Title Problems (see Title Ins, chap 2)	_____	_____	_____
9. Determine Required Endorsements (see Title Ins, chap 7)	_____	_____	_____
a. Owner's 100	_____	_____	_____
b. Subdivision	_____	_____	_____
c. Encroachments	_____	_____	_____
d. Survey	_____	_____	_____
e. Access	_____	_____	_____
f. Inflation	_____	_____	_____
g. Binder	_____	_____	_____
h. Bankruptcy exclusions	_____	_____	_____
10. Obtain Pro Forma Title Policy (see Title Ins, chap 10)	_____	_____	_____
11. Open Escrow (see chap 15)	_____	_____	_____
a. Deliver deposit	_____	_____	_____
b. Specify investments for deposit	_____	_____	_____
c. Select escrow agent	_____	_____	_____
d. Obtain reinsurance if necessary	_____	_____	_____
B. Debt Financing (on financing, see chap 4; California Real Estate Finance Practice: Strategies and Forms, chap 1 (Cal CEB 2000))			
1. Determine If Debt Financing Is Necessary	_____	_____	_____
a. Construction loan	_____	_____	_____
b. Takeout loan	_____	_____	_____
2. Determine If Existing Loan Is Assumable	_____	_____	_____
a. Review existing loan documents	_____	_____	_____
b. Negotiate assumption agreement	_____	_____	_____
3. Determine Availability of Bond Financing, Redevelopment Funds, or Similar Financing	_____	_____	_____
4. Consider Seller Financing (see chap 9)	_____	_____	_____
5. Consider Secondary Financing	_____	_____	_____

6. Prepare Lender Package	_____	_____	_____
7. Contact Lenders	_____	_____	_____
8. Negotiate Terms and Loan Application (see Real Estate Finance, chap 1)	_____	_____	_____
a. Rate, term, amount	_____	_____	_____
b. Nonrecourse/guarantees	_____	_____	_____
c. Transfer/assumption rights	_____	_____	_____
d. Other terms	_____	_____	_____
9. Negotiate Loan Commitment (see Real Estate Finance, chap 2)	_____	_____	_____
a. Commitment fee	_____	_____	_____
(1) Cash	_____	_____	_____
(2) Letter of credit	_____	_____	_____
b. Conditions for funding	_____	_____	_____
10. Approve or Disapprove Financing Contingency	_____	_____	_____
C. Equity Financing			
1. Determine If Equity Financing Is Necessary	_____	_____	_____
2. Identify Possible Equity Sources	_____	_____	_____
3. Identify Possible Equity Structures	_____	_____	_____
4. Consider Seller as Equity Source	_____	_____	_____
5. Consider Ground Lease Structure for Equity	_____	_____	_____
6. Consider Sale/Leaseback	_____	_____	_____
7. Prepare Package for Equity Financing	_____	_____	_____
8. Negotiate Equity Documents	_____	_____	_____
9. Obtain Firm Commitment	_____	_____	_____
10. Approve or Disapprove Financing Contingency	_____	_____	_____
11. Consider Pre-Sale	_____	_____	_____
D. Environmental (see §§1.64, 1.82, 1.88)			
1. Retain Environmental Engineer or Consultant	_____	_____	_____
2. Conduct and Review Phase I Investigation	_____	_____	_____
3. Conduct and Review Phase II Investigation	_____	_____	_____
4. Deliver Environmental Reports to:	_____	_____	_____
a. Prospective lenders	_____	_____	_____
b. Prospective equity participants	_____	_____	_____

c. Seller	_____	_____	_____
5. Prepare Response to Environmental Reports	_____	_____	_____
a. Prepare remediation plan	_____	_____	_____
b. Renegotiate seller's cleanup obligations	_____	_____	_____
c. Obtain clearance from necessary agencies	_____	_____	_____
d. Consider closure of underground tanks	_____	_____	_____
e. Obtain third party commitment to remediate	_____	_____	_____
f. Obtain remediation cost bid	_____	_____	_____
6. Approve or Disapprove Environmental Contingency	_____	_____	_____
E. Lease and Contract Review (see chap 4)			
1. Obtain and Review the Following Documents:	_____	_____	_____
a. Rent roll	_____	_____	_____
b. All leases and lease amendments	_____	_____	_____
c. All lease guarantees and subleases	_____	_____	_____
d. Lease concessions	_____	_____	_____
e. Tenant and guarantor financial statements	_____	_____	_____
f. Gross sales reports	_____	_____	_____
g. Current rent delinquency report	_____	_____	_____
h. Historical rent delinquency report	_____	_____	_____
i. Any executed letters of intent	_____	_____	_____
j. Most recent leasing status report	_____	_____	_____
k. Standard form lease	_____	_____	_____
l. All service and maintenance contracts	_____	_____	_____
m. All management contracts	_____	_____	_____
n. All warranties and guarantees	_____	_____	_____
2. Prepare Estoppels for Leases and Contracts (for form tenant estoppel, see App K)	_____	_____	_____
3. Deliver, Receive, and Review Estoppels	_____	_____	_____
4. Approve or Disapprove Estoppel Contingency	_____	_____	_____
5. Obtain Subordination Agreements for New Lender	_____	_____	_____
6. Determine Which Contracts Will Be Terminated	_____	_____	_____

7. Renegotiate Tenant Leases	_____	_____	_____
8. Conduct Manager and Contractor Interviews	_____	_____	_____
9. Approve or Disapprove Lease Contingency	_____	_____	_____
F. Financial Analysis (see §1.91)			
1. Review and Approve the Following:	_____	_____	_____
a. Historical financial statements	_____	_____	_____
b. Year-to-date unaudited financial statements	_____	_____	_____
c. Current operating and capital budgets	_____	_____	_____
d. Historical capital expenditures	_____	_____	_____
e. Real estate tax bills (including assessments)	_____	_____	_____
f. Aged receivables report	_____	_____	_____
g. Insurance policies now in effect	_____	_____	_____
h. Claims under insurance policies	_____	_____	_____
2. Prepare Pro Forma Budgets and Cash Flows	_____	_____	_____
3. Analyze Value on Cost, Comparable, and Other Bases	_____	_____	_____
4. Approve or Disapprove Economic Contingency	_____	_____	_____
G. Physical Inspections (see chap 4)			
1. Determine Gross and Net Acreage	_____	_____	_____
2. Inspect Physical Improvements	_____	_____	_____
a. Obtain and review the following reports:	_____	_____	_____
(1) Engineering reports	_____	_____	_____
(2) Mechanical reports, including HVAC	_____	_____	_____
(3) Roof reports	_____	_____	_____
(4) Asbestos reports	_____	_____	_____
(5) Seismographic reports	_____	_____	_____
(6) Existing plans and specifications	_____	_____	_____
(7) Americans with Disabilities Act (ADA) reports	_____	_____	_____
(8) Architect's review	_____	_____	_____
(9) Structural engineer reports	_____	_____	_____
(10) Contract's reports	_____	_____	_____
(11) Fire code reports	_____	_____	_____
b. Review public records re violations	_____	_____	_____
c. Analyze feasibility of planned			

modifications	_____	_____	_____
(1) Discuss with building and planning agencies	_____	_____	_____
(2) Process permit	_____	_____	_____
d. Inspect parking areas	_____	_____	_____
e. Determine compliance with Uniform Building Code (UBC) and zoning	_____	_____	_____
f. Obtain inspection by insurance company	_____	_____	_____
g. Obtain personal property inventory	_____	_____	_____
h. Perform UCC-3 search	_____	_____	_____
i. Approve or disapprove inspection contingency	_____	_____	_____
3. Inspect Nature of Land	_____	_____	_____
a. Topography	_____	_____	_____
b. Soils	_____	_____	_____
c. Obtain and review soils report	_____	_____	_____
d. Special conditions/cost	_____	_____	_____
e. Drainage	_____	_____	_____
(1) Any special requirements	_____	_____	_____
(2) Cost of such requirements	_____	_____	_____
4. Inspect Vegetation	_____	_____	_____
a. Usefulness	_____	_____	_____
b. Sensitivity	_____	_____	_____
5. Inspect Natural Water	_____	_____	_____
a. Usefulness	_____	_____	_____
b. Flood hazard	_____	_____	_____
c. Sensitivity	_____	_____	_____
d. Water table	_____	_____	_____
6. Mineral Rights	_____	_____	_____
7. Special Hazards	_____	_____	_____
a. Erosion potential	_____	_____	_____
b. Subsidence potential	_____	_____	_____
c. Fault zones potential	_____	_____	_____
d. Noise/vibration	_____	_____	_____
e. Toxics/chemicals	_____	_____	_____
f. Existing underground tanks	_____	_____	_____
g. Unsightly neighbors	_____	_____	_____
h. High winds	_____	_____	_____
i. Incompatibly zoned neighbors	_____	_____	_____
8. Accessibility	_____	_____	_____

a. Frontage/access streets	_____	_____	_____
b. Ability to handle projected traffic	_____	_____	_____
(1) Necessity for new signals	_____	_____	_____
(2) Necessity for road expansion	_____	_____	_____
c. Distance to major freeway	_____	_____	_____
d. Distance to shopping	_____	_____	_____
(1) Convenience shopping	_____	_____	_____
(2) Regional shopping	_____	_____	_____
e. Fire access	_____	_____	_____
9. Solicit Local Advice	_____	_____	_____
a. Seller(s)	_____	_____	_____
b. Local civil/soils engineers	_____	_____	_____
c. Planning/public works	_____	_____	_____
d. Architects	_____	_____	_____
e. Others	_____	_____	_____
10. Utilities	_____	_____	_____
a. Water	_____	_____	_____
(1) Availability	_____	_____	_____
(2) Sufficient quantity/pressure	_____	_____	_____
(3) Hook-up charges (fees)	_____	_____	_____
(4) Separation of fire and domestic supply	_____	_____	_____
b. Sewer	_____	_____	_____
(1) Adequate supplies to the site?	_____	_____	_____
(2) Hook-up charges (fees)	_____	_____	_____
c. Gas/electric	_____	_____	_____
(1) Availability	_____	_____	_____
(2) Cost to make available	_____	_____	_____
(3) Fees (how much, who pays)	_____	_____	_____
d. Telephone	_____	_____	_____
(1) Availability	_____	_____	_____
(2) Cost to make available	_____	_____	_____
(3) Fees (how much, who pays)	_____	_____	_____
e. Cable TV/satellite dish	_____	_____	_____
f. Storm drains/flood control	_____	_____	_____
(1) Cost	_____	_____	_____
11. Existing Approvals	_____	_____	_____
a. Review the following:	_____	_____	_____
(1) All licenses, permits and approvals	_____	_____	_____
(2) Certificates of occupancy	_____	_____	_____

(3) Copies of any notices of violations of law	_____	_____	_____
(4) List of litigation pending against property	_____	_____	_____
(5) Conditional use permits	_____	_____	_____
(6) Pending Environmental Impact Reports (EIRs)	_____	_____	_____
b. Obtain estoppels from local agencies	_____	_____	_____
c. Obtain new permits required for redevelopment	_____	_____	_____
H. Governmental Due Diligence (see §§1.72-1.90)			
1. Analyze Political Situation	_____	_____	_____
a. Politics of the city	_____	_____	_____
b. Politics of the site	_____	_____	_____
c. Neighborhood politics	_____	_____	_____
2. Analyze City Submission Process	_____	_____	_____
a. Type and steps	_____	_____	_____
3. Analyze Zoning/Density	_____	_____	_____
a. Present zoning	_____	_____	_____
b. Likely density	_____	_____	_____
c. Planned changes	_____	_____	_____
d. Procedure for changing	_____	_____	_____
e. Attitude of city officials towards changing	_____	_____	_____
4. Determine Attitude of Neighbors	_____	_____	_____
5. Investigate Growth Restrictions	_____	_____	_____
a. Existing	_____	_____	_____
b. Proposed	_____	_____	_____
c. Attitudes	_____	_____	_____
(1) City officials	_____	_____	_____
(2) Citizens	_____	_____	_____
6. Investigate Planning/Building Requirements	_____	_____	_____
a. Parking	_____	_____	_____
b. Design criteria	_____	_____	_____
c. Setbacks	_____	_____	_____
d. Special requirements/restrictions	_____	_____	_____
e. Landscaping	_____	_____	_____
f. Height	_____	_____	_____
g. Condo vs. apartment requirements	_____	_____	_____
h. Sprinklers	_____	_____	_____

i. ADA requirements	_____	_____	_____
j. Sound wall requirements	_____	_____	_____
k. Solar requirements	_____	_____	_____
l. Security requirements	_____	_____	_____
m. Seismic requirements	_____	_____	_____
7. Low/Moderate Income Requirements	_____	_____	_____
8. Public Use Requirements	_____	_____	_____
a. Fire station	_____	_____	_____
b. Open space, parks, roadway, school, etc.	_____	_____	_____
c. Any condemnation likely?	_____	_____	_____
d. Historical/archaeological	_____	_____	_____
e. Wildlife/environment	_____	_____	_____
f. Flood/fire/earthquake	_____	_____	_____
9. Investigate Subdivision Requirements	_____	_____	_____
a. Steps required	_____	_____	_____
b. Maps required	_____	_____	_____
c. Timing	_____	_____	_____
d. Special requirements	_____	_____	_____
10. Investigate City Fees	_____	_____	_____
a. Building/permits	_____	_____	_____
b. Subdivision/site development	_____	_____	_____
c. Planning/zoning	_____	_____	_____
d. Utility	_____	_____	_____
(1) Sewers	_____	_____	_____
(2) Water	_____	_____	_____
(3) Electrical/gas	_____	_____	_____
(4) Storm drains	_____	_____	_____
e. Parks	_____	_____	_____
f. Roads/traffic	_____	_____	_____
g. Schools	_____	_____	_____
h. Special fees	_____	_____	_____
i. Special assessments	_____	_____	_____
j. Tree fee	_____	_____	_____
k. Street lighting	_____	_____	_____
l. Underground signaling	_____	_____	_____
m. Housing mitigation fees	_____	_____	_____
n. Flood control	_____	_____	_____
o. Engineering/inspection	_____	_____	_____

p. Special taxes	_____	_____	_____
q. Growth management fees	_____	_____	_____
11. Review Off-Site Improvements	_____	_____	_____
a. Storm drainage	_____	_____	_____
b. Road improvement	_____	_____	_____
c. Flood control	_____	_____	_____
d. Parks improvements	_____	_____	_____
e. Special facilities	_____	_____	_____
f. Traffic signals	_____	_____	_____
g. Sanitary	_____	_____	_____
h. Underground utilities	_____	_____	_____
i. Sidewalks	_____	_____	_____
12. Analyze Possible Development Agreements	_____	_____	_____
a. Are they available	_____	_____	_____
b. Is a long agreement required	_____	_____	_____
I. Negotiate New Leases			
1. Identify Prospective Tenants	_____	_____	_____
2. Obtain Seller Consent to Negotiate	_____	_____	_____
3. Draft Letter of Intent	_____	_____	_____
4. Draft New Leases	_____	_____	_____
J. Ground Leases			
1. Review and Approve Ground Leases	_____	_____	_____
2. Confirm Finance Ability	_____	_____	_____
3. Renegotiate	_____	_____	_____
4. Buy-Out Ground Lessor	_____	_____	_____
5. Get Ground Lessor Estoppel	_____	_____	_____
6. Draft and Obtain Ground Lessor Consent	_____	_____	_____
7. Prepare Form of Ground Lessor Assignment	_____	_____	_____
K. Obtain Board Approval (see §1.92)	_____	_____	_____
L. Other			
1. Obtain Appraisal	_____	_____	_____
2. Determine If Any Current or Threatened Litigation	_____	_____	_____
3. Determine If Any Current or Threatened Condemnation	_____	_____	_____

IV. CLOSING DUE DILIGENCE AND PROCEDURES

A. Prepare Partnership (or LLC) Agreement (see Advising California Partnerships (3d ed Cal CEB 1999))			

1. Determine Identity of Partners or Members	_____	_____	_____
2. Determine Capital Contributions	_____	_____	_____
3. Determine Percentage Interests	_____	_____	_____
4. Determine Voting Rights	_____	_____	_____
5. Determine Buy-Out Rights	_____	_____	_____
6. Reserve Partnership or LLC Name	_____	_____	_____
7. File LP-1	_____	_____	_____
8. Obtain Tax ID No.	_____	_____	_____
9. Draft Partnership or LLC Agreement	_____	_____	_____
10. Execute Partnership of LLC Agreement	_____	_____	_____
11. Deliver Partnership or LLC Agreement to Lender	_____	_____	_____
B. Prepare Final Closing Documents			
1. Grant Deed (see chap 10; for form, see App G)	_____	_____	_____
2. Bill of Sale (for form, see App H)	_____	_____	_____
3. Assignment of Leases (for form, see App I)	_____	_____	_____
4. Assignment of Intangibles (for form, see App J)	_____	_____	_____
5. Escrow Holdback Agreement	_____	_____	_____
6. Tax withholding Statements	_____	_____	_____
7. Loan Documents (see Real Estate Finance)	_____	_____	_____
8. Partnership Agreements (see Advising Partners)	_____	_____	_____
9. Loan Assumptions	_____	_____	_____
10. Authority Documents (for forms, see Apps D-F)	_____	_____	_____
11. Environmental Indemnity	_____	_____	_____
12. California Withholding Exemption Certificate (form 590)	_____	_____	_____
13. FIRPTA Statement	_____	_____	_____
14. Preliminary Change in Ownership Report	_____	_____	_____
C. Prepare Escrow Instructions (see chap 15)			
1. No Transfer Tax of Record	_____	_____	_____
2. Consider Minimization of Transfer Tax	_____	_____	_____
3. Deposit of Funds	_____	_____	_____
4. Condition Closing on Termination of Contracts	_____	_____	_____

5. Condition Closing on Final Buyer Inspection	_____	_____	_____
6. Confirm Seller Authority to Sign	_____	_____	_____
D. Approve Closing Statement (see §15.48)	_____	_____	_____
E. Finalize Title Policy	_____	_____	_____
F. Arrange for Wire Transfer of Funds	_____	_____	_____
G. Obtain Original Seller Materials			
1. Keys	_____	_____	_____
2. Original Leases and Contracts	_____	_____	_____
3. As-Builts and Other Plans	_____	_____	_____
4. Guarantees and Warranties	_____	_____	_____
5. Correspondence and Financial Records	_____	_____	_____
6. Other Original Material	_____	_____	_____
7. Security Deposits	_____	_____	_____
8. Permits and Certificate of Occupancy	_____	_____	_____
9. Other Books and Records	_____	_____	_____
H. Miscellaneous			
1. Termination Designated Contracts	_____	_____	_____
2. Send Notification Letter to Tenants (for form, see App L)	_____	_____	_____
3. Confirm no Change in Condition of Property	_____	_____	_____
4. Confirm Accuracy of Seller Representations	_____	_____	_____
I. Obtain and Put in Place:			
1. New Insurance Policies	_____	_____	_____
2. New Property Manager	_____	_____	_____
3. New Service Providers	_____	_____	_____
4. New Utility Service	_____	_____	_____
5. Terminate Designated Contracts	_____	_____	_____
V. AFTER CLOSING			
A. Prepare Closing Binder	_____	_____	_____
B. Arrange for Delivery of Executed Documents	_____	_____	_____
C. Obtain and Review Title Policy (see Title Ins, chap 11)	_____	_____	_____
D. Handle Post-Closing Prorations	_____	_____	_____
E. Consider Tax Reassessment	_____	_____	_____
VI. KEY CONTACTS			
1. Seller			

Name of entity:_____

Contact:_____

Address:_____

_____

Phone:_____

Fax:_____

2. Seller's Broker

Name of company:_____

Name of broker:_____

Address:_____

_____

Phone:_____

Fax:_____

3. Seller's Attorney

Name of Firm:_____

Name of Attorney:_____

Address:_____

_____

Phone:_____

Fax:_____

4. Buyer

Name of entity:_____

Contact:_____

Address:_____

_____

Phone:_____

Fax:_____

5. Buyer's Broker

Name of Company:_____

Name of Broker:_____

Address:_____

_____

Phone:_____

Fax:_____

6. Buyer's Attorney

Name of Firm:_____

Name of Attorney:_____

Address:_____

_____

Phone:_____

Fax:_____

7. Title Company

Name of Company:_____

Contact:_____

Address:_____

_____

Phone:_____

Fax:_____

8. Escrow Company

Name of Company:_____

Escrow Officer:_____

Escrow No.:_____

Address:_____

_____

Phone:_____

Fax:_____

9. Environmental Engineer

Name of Firm:_____

Name of Engineer:_____

Address:_____

_____

Phone:_____

Fax:_____

10. Contractor

Name of Firm:_____

Contact:_____

Address:_____

_____

Phone:_____

Fax:_____

11. Current Property Manager

Name of Company:_____

Name of Contact:_____

Address:_____

_____

Phone:_____

Fax:_____

12. Other

_____

_____

_____

_____

_____

_____

_____

_____

NOTE: In Northern California, the title company (7) and escrow company (8) are generally the same company, but there will be separate escrow and title officers.

© The Regents of the University of California

Appendix C

Checklist of Due Diligence Materials to Be Delivered by Seller to Buyer in Sale Involving Commercial Leases

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

Checklist of Due Diligence Materials to Be Delivered by Seller to Buyer in Sale Involving Commercial Leases

THIS IS A COMPREHENSIVE LIST AND NOT ALL MATERIAL IS REQUIRED IN EVERY TRANSACTION. THE ATTORNEY'S DUTY, IF ANY, TO COLLECT ANY OF THIS INFORMATION SHOULD BE DESCRIBED IN THE RETAINER AGREEMENT.

TENANT INFORMATION

___ 1. Rent roll showing, for each tenant, the tenant's name, suite number, size of premises, rent, rental increases, percentage rent, pro rata share, caps, security deposit, term, commencement and expiration dates, options, and other material provisions.

___ 2. All leases (including all exhibits and attachments) and amendments, including guarantees and subleases.

___ 3. Concessions made to tenants, including free or reduced rent, above standard tenant improvements, cash payments, moving allowances, or takeover of previous lease obligations.

___ 4. Most recent financial statements and credit information and reports, if any, on any tenant and of any guarantors of any leases or rents.

___ 5. Any executed letters of intent with prospective tenants.

___ 6. Most recent leasing status report from leasing broker.

___ 7. Standard form lease.

OPERATING INFORMATION

___ 1. Historical financial statements of the Property for calendar years (audited, if available), and for the current calendar year as soon as available.

___ 2. Year-to-date unaudited financial statements for the Property.

___ 3. Current operating and capital budgets of the Property, including comparison of actual to budgeted results and an explanation of significant variances.

___ 4. Listing of capital expenditures for the Property for the prior three (3) years.

___ 5. Copies of all service, maintenance, leasing, management, or other contracts, and all other agreements, warranties, and guaranties relating to the operation, use, management, or maintenance of the Property.

___ 6. Copies of real estate tax bills (including special assessments) for the prior three (3) years, including evidence of payment of each.

___ 7. Aged receivables report through the date of this Letter of Intent and monthly receivables reports for the prior twenty-four (24) months.

___ 8. Copies of all insurance policies now in effect with respect to the Property, copies of any claims under such

policies, and any evidence in Seller's possession that tenants are maintaining the insurance coverages required under their leases.

BUILDING INFORMATION

___ 1. Any engineering reports, including reports on foundation, walls, roofs, floors, and supports.

___ 2. Any mechanical reports, including HVAC.

___ 3. Any roof reports.

___ 4. Any environmental reports, including soils tests and asbestos reports.

___ 5. Any seismographic reports.

___ 6. Any plans and specifications showing "as built" condition of the Property.

___ 7. Any reports showing compliance with Americans with Disabilities Act (ADA) requirements.

___ 8. Any architect's certificate certifying the square footage of the building.

MISCELLANEOUS

___ 1. All licenses, permits, and approvals for the Property, including, without limitation, certificates of occupancy for the building and for each tenant.

___ 2. Most recent boundary and/or title survey.

___ 3. Most recent closing binder for the Property, including any current financing documents.

___ 4. Current owner's policy of title insurance for the Property.

___ 5. Recent photographs of the Property, if any.

___ 6. Copies of any notices of violations of any federal, state, municipal, or other health, fire, building, zoning, safety, environmental protection, or other applicable codes, laws, rules, regulations, or ordinances relating or applying to the Property.

___ 7. List of all litigation pending against the Property, against Seller, or any general partner of the Seller that relates to the Property.

___ 8. Ground Leases, reciprocal easement agreements, and other title matters.

© The Regents of the University of California

Appendix D

Board Resolution (Authorizing Purchase)

To download **Word** version, right click and choose *Save Target As*

To download **WordPerfect** version, right click and choose *Save Target As*

Resolution of Board of Directors of
_ _[*Name of corporation*]_ _

At a meeting of the board of directors of _ _[*name of corporation*]_ _ (Corporation), duly held on _ _[*date*]_ _, at which meeting all directors were in attendance, the following resolutions were unanimously adopted:

WHEREAS, the Corporation is about to enter into a _ _[*name of document*]_ _ (the Agreement), dated _ _[*date*]_ _, to purchase certain property located at _ _[*city*]_ _, California (the Property); and

WHEREAS, the Board of Directors of this Corporation has reviewed the Agreement and all documents executed or to be executed in connection with it and considers the transaction to be in the best interest of the Corporation.

NOW, THEREFORE, BE IT RESOLVED that this Corporation execute the Agreement and all documents previously presented to, reviewed, and approved by the Board of Directors of this Corporation and consummate the purchase of the Property.

RESOLVED, FURTHER, that the officers of this Corporation acting alone be, and they hereby are, authorized, empowered, and directed on behalf of this Corporation to execute and deliver the Agreement and all other documents to be executed in connection with it, and to take all actions that may be necessary to conclude the transaction contemplated by these documents. Those officers are the following:

President
_ _[*Name*]_ _

Secretary
_ _[*Name*]_ _

_ _[*Titles of other officers*]_ _
_ _[*Names*]_ _

The authority conferred by this resolution shall be considered retroactive, and any and all acts authorized in this resolution that were performed before the passage of this resolution are approved and ratified. The authority confirmed by this resolution shall continue in full force and effect until _ _[*name of seller*]_ _ shall have received notice in writing, certified by the Secretary of the Corporation, of the revocation of this authority by a resolution duly adopted by the board of directors of this Corporation.

The undersigned, _ _[*name*]_ _, Secretary of this Corporation, certifies that the foregoing is a true copy of the resolution duly adopted by the Board of Directors of this Corporation at a meeting held on _ _[*date*]_ _.

IN TESTIMONY WHEREOF, I have executed this resolution and affixed the corporate seal of the Corporation as of _ _[*date*]_ _.

Date: _ _ _ _ _ _

__[*Signature*]__
Name: _ _[*Typed name*]_ _
Secretary

[*Seal*]

Name: _ _[*Typed name*]_ _
_ _[*Title*]_ _

Name: _ _[*Typed name*]_ _
_ _[*Title*]_ _

© The Regents of the University of California

Appendix E

Limited Liability Company Certificate (Authorizing Purchase)

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

The undersigned members of _ _[*name of limited liability company*]_ _ (LLC), do certify that we are all of the members of the LLC and that there are no other members.

We further certify that any one (1) of the following named persons:

_ _[*Identify authorized signors*]_ _

be, and they are, authorized and empowered for and on behalf of and in the name of the LLC to execute and deliver a _ _[*name of document*]_ _, dated _ _[*date*]_ _, to purchase certain property located at _ _[*city*]_ _, California, and all other documents to be executed in connection with this purchase, and to take all actions that may be considered necessary to conclude the transaction contemplated by these documents.

The authority conferred shall be considered retroactive, and any and all acts authorized in this document that were performed before the execution of this certificate are approved and ratified. The authority conferred shall continue in full force and effect until _ _[*name of seller*]_ _ shall have received notice in writing from the LLC of the revocation of this certificate.

We further certify that the activities covered by the foregoing certifications constitute duly authorized activities of the LLC; that these certifications are now in full force and effect; and that there is no provision in any document under which _ _[*name of seller*]_ _ is organized and/or that governs the LLC's continued existence limiting the power of the undersigned to make the certifications set forth in this certificate, and that the same are in conformity with the provisions of all such documents.

Members:
__[*Signature of member*]__
_ _[*Typed name*]_ _

__[*Signature of member*]__
_ _[*Typed name*]_ _

__[*Signature of member*]__
_ _[*Typed name*]_ _

© The Regents of the University of California

Appendix F

Statement of Partnership Authority (Secretary of State Form GP-1)



GP-1

File # _____

Document # _____

State of California
Secretary of State

STATEMENT OF PARTNERSHIP AUTHORITY

A $70.00 filing fee must accompany this form.

IMPORTANT – Read instructions before completing this form.

This Space For Filing Use Only

PARTNERSHIP NAME

1. NAME OF PARTNERSHIP

OFFICE ADDRESSES (Do not abbreviate the city. Items 2 and 3 cannot be P.O. Boxes.)

2. STREET ADDRESS OF CHIEF EXECUTIVE OFFICE	CITY AND STATE		ZIP CODE
3. STREET ADDRESS OF CALIFORNIA OFFICE, IF ANY	CITY	STATE **CA**	ZIP CODE

NAMES & ADDRESSES OF PARTNERS (Complete Item 4 with the names and mailing addresses of all the partners (attach additional pages if necessary) **OR** leave Item 4 blank and proceed to Item 5. Any attachments to this document are incorporated herein by this reference.)

4. NAME	ADDRESS	CITY AND STATE	ZIP CODE
NAME	ADDRESS	CITY AND STATE	ZIP CODE
NAME	ADDRESS	CITY AND STATE	ZIP CODE

APPOINTED AGENT (If Item 4 was not completed, complete Item 5 with the name and mailing address of an agent appointed and maintained by the partnership who will maintain a list of the names and mailing addresses of all the partners. If Item 4 was completed, leave Item 5 blank and proceed to Item 6.)

5. NAME	ADDRESS	CITY AND STATE	ZIP CODE

AUTHORIZED PARTNERS (Enter the name(s) of all the partners authorized to execute instruments transferring real property held in the name of the partnership. Attach additional pages if necessary. Any attachments to this document are incorporated herein by this reference.)

6. PARTNER NAME:	PARTNER NAME:
PARTNER NAME:	PARTNER NAME:
PARTNER NAME:	PARTNER NAME:

ADDITIONAL INFORMATION

7. ADDITIONAL INFORMATION SET FORTH ON THE ATTACHED PAGES, IF ANY, IS INCORPORATED HEREIN BY THIS REFERENCE AND MADE PART OF THIS DOCUMENT.

EXECUTION (If additional signature space is necessary, the dated signature(s) with verification(s) may be made on an attachment to this document. Any attachments to this document are incorporated herein by this reference.)

8. I CERTIFY UNDER PENALTY OF PERJURY UNDER THE LAWS OF THE STATE OF CALIFORNIA THAT THE FOREGOING IS TRUE AND CORRECT OF MY OWN KNOWLEDGE.

SIGNATURE OF PARTNER	DATE	TYPE OR PRINT NAME OF PARTNER	
SIGNATURE OF PARTNER	DATE	TYPE OR PRINT NAME OF PARTNER	

Print

INSTRUCTIONS FOR COMPLETING THE STATEMENT OF PARTNERSHIP AUTHORITY (FORM GP-1)

For easier completion, this form is available on the Secretary of State's website at http://www.ss.ca.gov/business and can be viewed, filled in and printed from your computer. The completed form can be mailed to Secretary of State, Document Filing Support Unit, P.O. Box 944225, Sacramento, CA 94244-2250 or delivered in person to the Sacramento office, 1500 11th Street, 3rd Floor, Sacramento, CA 95814. If you are not completing this form online, please type or legibly print in black or blue ink. This form should not be altered. This form is only filed in the Sacramento office.

Statutory filing provisions are found in California Corporations Code section 16303. All statutory references are to the California Corporations Code, unless otherwise stated.

- Unless otherwise provided in the Partnership Agreement, a person who files a Statement of Partnership Authority (Form GP-1) pursuant to Section 16105 shall promptly send a copy of the statement to every non-filing partner and to any other person named as a partner in the statement. (Sections 16103(b)(1) and 16105(e).)

- In order for a statement to be effective for real estate transfers, a certified copy of the statement issued by the Secretary of State must be recorded in the office for recording transfers of real properly. (Section 16105(b).)

FEES: The fee for filing Form GP-1 is $70.00. There is an additional $15.00 special handling fee for processing a document delivered in person to the Sacramento office. The special handling fee must be remitted by separate check for each submittal and will be retained whether the document is filed or rejected. The preclearance and/or expedited filing of a document within a guaranteed time frame can be requested for an additional fee (in lieu of the special handling fee). Please refer to the Secretary of State's website at http://www.ss.ca.gov/business/precexp.htm for detailed information regarding preclearance and expedited filing services. The special handling fee or preclearance and expedited filing services are not applicable to documents submitted by mail. Check(s) should be made payable to the Secretary of State.

COPIES: The Secretary of State will certify two copies of the filed document(s) without charge, provided that the copies are submitted to the Secretary of State with the document(s) to be filed. Any additional copies submitted will be certified upon request and payment of the $8.00 per copy certification fee.

Complete Form GP-1 as follows:

Item 1. Enter the name of the partnership.

Item 2. Enter the complete street address, including the zip code, of the chief executive office of the general partnership. Please do not enter a P.O. Box or abbreviate the name of the city.

Item 3. Enter the complete street address of an office in California if the chief executive office entered in Item 2 is not located in California. Please do not enter a P.O. Box or abbreviate the name of the city.

Items 4 & 5. The partnership must provide either of the following: (Item 4) the names and mailing addresses of all of the partners; OR (Item 5) the name and mailing address of an agent appointed and maintained by the partnership to provide the names and mailing addresses of all the partners pursuant to the provisions of Section 16303(b). Attach additional pages, if necessary.

Item 6. Enter the names of all partners authorized to execute instruments transferring real property held in the name of the partnership. Attach additional pages, if necessary.

Item 7. Attach any other information to be included in the Statement of Partnership Authority, provided that the information is not inconsistent with law.

Item 8. Form GP-1 must be executed by at least two partners. (Section 16105(c).) If additional signature space is necessary, the signatures may be made on an attachment to the document.

Any attachments to Form GP-1 are incorporated by reference. All attachments should be 8 ½" x 11", one-sided and legible.

© The Regents of the University of California

Appendix G

Grant Deed

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

RECORDING REQUESTED BY

AND WHEN RECORDED MAIL TO:

_ _[*Name*]_ _

_ _[*Address*]_ _

MAIL TAX STATEMENTS TO:

_ _[*Name*]_ _

_ _[*Address*]_ _

Documentary Transfer Tax amount not shown pursuant to Revenue & Taxation Code Section 11932

City of _ _[*name*]_ _, County of _ _[*name*]_ _, State of California

GRANT DEED

By this instrument dated _ _[*date*]_ _, for a valuable consideration, _ _[*name*]_ _, a _ _[*e.g., California corporation*]_ _ (Grantor), grants to _ _[*name*]_ _, a _ _[*e.g., California corporation*]_ _ (Grantee), certain real property situated in the State of California, County of _ _[*name*]_ _, more particularly described in Exhibit A attached to this Deed and incorporated in it by this reference, subject, however, to: (a) taxes and assessments, both general and special, not now due and payable; (b) building and zoning ordinances, laws, regulations and restrictions by municipal or other governmental authority; (c) any and all leases, easements, rights-of-way, encumbrances, conditions, covenants, restrictions, reservations and exceptions of record; and (d) all matters including, but not limited to, road, highway, pipeline, railroad and utility easements which would be disclosed by a survey and inspection of the property.

Grantor, for the same consideration, acknowledges its intention to convey by this Deed not only all present right, title, and interest but also any and all right, title, and interest after-acquired by Grantor or its assigns in the above-described property.

The officers who sign this Deed on behalf of Grantor certify that this Deed and transfer represented by this Deed was duly authorized by resolution of Grantor.

Executed on _ _[*date*]_ _

GRANTOR _ _[*Name of corporation*]_ _,
a _ _[*state of incorporation*]_ _ **corporation**

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

[*ALL SIGNATURES MUST BE ACKNOWLEDGED*]

TRANSFER DECLARATION

DO NOT RECORD

County Recorder

_ _[*Name*]**_ _ County, California**

It is requested that this Declaration of Documentary Transfer Tax not be recorded with the attached Grant Deed, but be affixed to the Grant Deed after it is recorded and before it is returned.

The Grant Deed names _ _[*name*]**_ _ as Grantor and _ _**[*name*]**_ _ as Grantee. The property being transferred is located in the City of _ _**[*name*]**_ _, County of _ _**[*name*]**_ _, State of California. The Assessor's Parcel No. is _ _**[*number*]**_ _.**

The undersigned Grantor declares that the amount of Documentary Transfer Tax due on the attached Grant Deed is _ _[*dollar amount*]**_ _, computed on the full value _ _**[*of the interest or property conveyed*]**_ _ _ _**[*less the value of liens and encumbrances remaining at the time of sale*]**_ _.**

I declare under penalty of perjury that the foregoing is true and correct.

Date: _ _ _ _ _ _

_ _[*Name of corporation*]**_ _,**
a _ _[*state of incorporation*]**_ _ corporation**

By: __[*Signature*]**__**
Name: _ _[*Typed name*]**_ _**
Its: _ _[*Title*]**_ _**

© The Regents of the University of California

Appendix H

Bill of Sale

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

FOR VALUABLE CONSIDERATION, receipt of which is acknowledged by execution of this document, the undersigned, _ _[*name*]_ _, a _ _[*e.g., California corporation*]_ _ (Owning Entity) does on _ _[*date*]_ _, grant, convey, transfer, assign, bargain, sell, deliver, and set over unto _ _[*name*]_ _, a _ _[*e.g., California corporation*]_ _, its successors and assigns (Acquiror), forever, all of the Owning Entity's right, title, and interest in and to the following personal property located in and upon and used in connection with the operation of all the improvements (Improvements) on the land located in _ _[*city*]_ _, California, generally known as _ _[*e.g., The Smith Building/1000 Smith Road*]_ _, as more particularly described on Exhibit A attached to this document (the Land): (a) all appliances, parts, instruments, equipment, personal property, appurtenances, accessories, furnishings, fixtures, and other property owned by Owning Entity and incorporated or installed in or on and used in connection with the operation of the Improvements or attached to the Land and including without limitation any reports, plans, renderings, permits, approvals, and maps related to the Improvements or Land, (collectively, the Personal Property), and (b) all warranties, guaranties and indemnities, whether those warranties, guaranties, and indemnities are express or implied, and all similar rights that Owning Entity may have against any manufacturer, supplier, seller, engineer, contractor, or builder, in respect of the Personal Property, or any portion of the Personal Property (collectively, Warranties).

Owning Entity does represent and warrant to Acquiror that Owning Entity is the lawful owner of the Personal Property and the Warranties and that the Personal Property and the Warranties are free and clear from all liens and encumbrances. Owning Entity shall indemnify, defend, and hold Acquiror harmless from and against any and all claims, demands, costs, liabilities, losses, damages, penalties, or expenses of any kind, including without limitation attorney and expert witness fees that may be brought or made against Acquiror or that Acquiror may incur by reason of any defect in Owning Entity's title to the Personal Property or in the Warranties as represented and warranted in this document, or as a result of a lien or encumbrance on the Personal Property.

[*If appropriate, add following Seller provision*]

Except as set forth in the preceding paragraph, the sale of the Personal Property is on an "as is," "with all faults" basis and without any warranty or representation, express or implied, of any nature or sort, including, without limitation, any warranty of merchantability, fitness of use for a particular purpose, or otherwise.

[*Continue*]

This Bill of Sale shall in all respects be governed by, and construed in accordance with the laws of the State of California, including all matters of construction, validity, and performance.

IN WITNESS WHEREOF, Owning Entity has caused this Bill of Sale to be duly executed and delivered on the day and year specified above.

Date: _ _ _ _ _ _

_ _[*Name of corporation*]_ _,
a _ _[*state of incorporation*]_ _ **corporation**

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

© The Regents of the University of California

Appendix I

Assignment of Leases

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

RECORDING REQUESTED BY

_ _[*Name*]_ _

WHEN RECORDED, RETURN TO:

_ _[*Name*]_ _

_ _[*Address*]_ _

ASSIGNMENT OF LEASES

THIS ASSIGNMENT OF LEASES (Assignment) is executed as of _ _[*date*]_ _ by and between, _ _[*name*]_ _, a _ _[*e.g., California corporation*]_ _ (Assignor) and _ _[*name*]_ _, a _ _[*e.g., California corporation*]_ _ (Assignee).

RECITALS

A. Assignor, as owner of the real property and the improvements on it (collectively, the Property), located in the County of _ _[*name*]_ _, California, and more thoroughly described in attached Exhibit A, is the landlord under the leases (the Leases) described in attached Exhibit B that cover portions of the Property.

B. Assignor is contributing to Assignee and Assignee is acquiring from Assignor all of Assignor's right, title, and interest in and to the Property. In connection therewith, Assignor desires to assign to Assignee, and Assignee desires to accept the assignment of, all of Assignor's right, title, and interest in and to the Leases, all on the terms and conditions set forth below.

NOW, THEREFORE, in consideration of the foregoing recitals and the mutual covenants and conditions contained in them, the parties agree as follows:

1. Assignment. Assignor assigns, transfers, and conveys to Assignee all of Assignor's right, title, and interest in and to the Leases together with all of the rents, income, receipts, revenues, issues, profits, security deposits, prepaid rents, and all other benefits arising or issuing from or out of the Leases, and together with any and all rights that Assignor may have against the tenants under the Leases, or any of them.

2. Assumption. Assignee hereby assumes all of Assignor's obligations under the Leases subsequent to the date of this Assignment and shall indemnify and defend Assignor against and hold Assignor from any and all losses, costs, damages, liabilities, and expenses, including, without limitation, reasonable attorney fees, incurred by Assignor as a result of any claim arising under any of the Leases and based on events occurring subsequent to the date of this Assignment.

3. Indemnity. Assignor shall indemnify and defend Assignee against and hold Assignee harmless from any and all losses, costs, damages, liabilities, and expenses, including, without limitation, reasonable attorney fees, incurred by Assignee as a result of any claim arising under any of the Leases and based on events occurring on or before the date of this Assignment.

4. Warranties of Assignor. Assignor warrants, represents, and covenants to Assignee, to the best of Assignor's knowledge, as to each Lease, as follows:

(a) There are and will be no oral or written agreements with respect to any Lease allowing the tenant any reduction, abatement, concession, allowance, or subsidy of rent under its Lease or allowing the payment of any portion of the rent in any form other than in cash except as may be fully noted on the rent roll delivered to Assignee;

(b) No rentals or other payments for periods in excess of one month have been received under any Lease except as reflected on the rent roll;

(c) Assignor is not in violation of any Lease;

(d) There is no prohibition set forth in any Lease with respect to Assignor's assignment of such Lease;

(e) All painting, repairs, alterations, and other work to be performed by the landlord under each Lease have been fully performed by the Landlord under each Lease and have been fully paid or will be fully performed and paid on or before the closing date; and

(f) No brokerage or leasing commission or other compensation will be due and payable to any person, firm, corporation, or other entity with respect to or on account of any such Lease (Assignor shall fully pay any such commissions or compensation as they come due, and Assignor and each partner of Assignor shall indemnify, defend, and hold Assignee harmless from any and all such commissions or compensation).

5. No Partnership. None of the terms and conditions of this Assignment shall create a partnership between or among the parties to this Assignment and their respective businesses or otherwise, nor shall it cause them to be considered joint venturers or members of any joint enterprise. This Assignment is not intended, nor shall it be construed, to create any third-party beneficiary rights in any person who is not a party to this Assignment, including without limitation any tenant under a Lease.

6. Severability. If any term of this Assignment or the application of such term to a person or circumstance shall to any extent be declared invalid or unenforceable, the remainder of this Assignment, or the application of such term to persons or circumstances other than those to which it is invalid or unenforceable, shall not be affected by it, and each term of this Assignment shall remain valid and enforceable to the fullest extent permitted by law.

7. Heirs. This Assignment shall be binding on and inure to the benefit of the parties and their respective heirs, legal and personal representatives, successors, and assigns.

8. Attorney Fees. If a dispute arises concerning the performance of the obligations under this Assignment or the meaning or interpretation of any provision of this Assignment, the party not prevailing in the dispute shall pay any and all costs and expenses incurred by the other party in establishing its rights under this assignment, including, without limitation, court costs and reasonable attorney fees.

IN WITNESS WHEREOF, the parties hereto have executed this Assignment on the date first above written.

Assignor: _ _[*Name of corporation*]_ _,
a _ _[*state of incorporation*]_ _ **corporation**

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

Assignee: _ _[*Name of corporation*]_ _,
a _ _[*state of incorporation*]_ _ **corporation**

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

[*ALL SIGNATURES MUST BE ACKNOWLEDGED*]

© The Regents of the University of California

Appendix J

Assignment of Intangibles

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

RECORDING REQUESTED BY

_ _[*Name*]_ _

WHEN RECORDED, RETURN TO:

_ _[*Name*]_ _

_ _[*Address*]_ _

ASSIGNMENT OF INTANGIBLES

THIS ASSIGNMENT OF INTANGIBLES (the Intangible Property Assignment) is entered into as of _ _[*date*]_ _ by and between _ _[*name*]_ _ a _ _[*e.g., California corporation*]_ _ (Assignor), and _ _[*name*]_ _, a _ _[*e.g., California corporation*]_ _ (Assignee).

RECITALS

The parties enter into this Intangible Property Assignment on the basis of the following facts, understandings, and intentions:

A. Assignor, as the owner of the land and improvements located at _ _[*address*]_ _, California, as more particularly described in attached Exhibit A (Property), is party to, holder of, or owner of those certain contracts, agreements, guarantees, warranties, licenses, permits, consents, approvals, and other documents of every kind and nature relating to, utilized in connection with, necessary to, or appropriate for the operation of the Property, including without limitation all of the following: (1) all equipment leases, rental agreements, and similar financing agreements concerning any item of Personal Property described on attached Exhibit B (collectively, the Equipment Leases); (2) all contracts or agreements for the service, maintenance, and operation of the Property, including without limitation supply contracts, utility service agreements, trash disposal contracts, maintenance and repair contracts, janitorial service contracts, landscaping maintenance agreements, and license and concession agreements and every other contract described on attached Exhibit C (collectively, the Service Contracts); (3) all licenses, franchises, registrations, certificates, approvals, and permits, issued by governmental authorities or quasi-governmental authorities and required for the occupancy, maintenance, or operation of the Property or any part of the Property, including building pads, certificates of occupancy, and business licenses described on attached Exhibit D (collectively, the Permits) (all of the items described in clauses (1) through (3) of this Recital A shall collectively be referred to as the Contracts); (4) names commonly used in the operation of the Property, together with the goodwill appurtenant to those names (collectively, the Names); (5) all contract rights, trademarks, logos, copyrights, and other items of tangible or intangible personal property relating to the ownership or operation of the Property (collectively, the Miscellaneous Assets); and (6) any condemnation or insurance award or other awards now pending or made after the close of escrow or Assignee's acquisition of the Property, by any private entity or any municipal, county, state, or federal authority or board with respect to the Property (collectively, Awards).

B. Assignor is contributing to Assignee and Assignee is acquiring from Assignor any and all of Assignor's right, title, and interest in and to the Property. With the execution of this Assignment, Assignor is assigning to Assignee all Assignor's right, title, and interest in the Contracts, Names, Miscellaneous Assets, and Awards

(collectively, the Intangible Property). In connection with the acquisition and contribution of Assignor's interest in the Property, Assignor desires to assign to Assignee and Assignee desires to accept the assignment of all of Assignor's right, title, and interest in and to the Intangible Property, and Assignee desires to assume all of Assignor's obligations, all on the terms and conditions set forth below.

NOW, THEREFORE, in consideration of the foregoing recitals and the mutual covenants and conditions contained in them, the parties agree as follows:

1. Assignment. Effective as of the date of this Intangible Property Assignment, Assignor assigns, transfers, and conveys to Assignee all of Assignor's right, title, and interest in and to the Intangible Property.

2. Acceptance. Assignee accepts the foregoing assignment and assumes all obligations under the Service Contracts and Equipment Leases to the extent these obligations relate to the period on or after the date of this Intangible Property Assignment.

3. Indemnity. Assignor shall indemnify, protect, and defend Assignee against and hold Assignee harmless from any and all losses, costs, damages, liabilities and expenses, including attorney fees, incurred by Assignee as a result of any claim of any third party arising with respect to an event or alleged default, action, omission, or negligence of Assignor or its employees, agents, guests, or invitees, occurring on or before the date of this Assignment in connection with any of the Intangible Property. Assignee shall indemnify, protect, and defend Assignor against and hold Assignor harmless from any and all losses, costs, damages, liabilities, and expenses, including attorney fees, incurred by Assignor as a result of any claim of any third party arising with respect to an event or alleged default, action, omission, or negligence of Assignee or its employees, agents, guests, or invitees, occurring after the date of this Intangible Property Assignment in connection with any of the Intangible Property.

4. Severability. If any term of this Intangible Property Assignment or its application to a person or circumstance shall to any extent be declared invalid or unenforceable, the remainder of this Intangible Property Assignment or the application of the term to persons or circumstances other than those to which it is invalid or unenforceable shall not be affected, and each term of this Intangible Property Assignment shall remain valid and enforceable to the fullest extent permitted by law.

5. Partnership. None of the terms and conditions of this Intangible Property Assignment shall create a partnership between the parties and their respective businesses or otherwise, nor shall it cause them to be considered joint venturers or members of any joint enterprise. This Intangible Property Assignment is not intended, nor shall it be construed, to create any third-party beneficiary rights in any person who is not a party to it, including other parties to the Contracts.

6. Attorney Fees. If a dispute arises concerning the performance of obligations under this Intangible Property Assignment or the meaning or interpretation of any provision of it, the party not prevailing in the dispute shall pay any and all costs and expenses incurred by the other party in establishing its rights under this Intangible Property Assignment, including costs and reasonable attorney and expert witness fees.

7. Successors and Assigns. This Intangible Property Assignment shall be binding on and inure to the benefit of the parties and their successors and assigns.

8. Governing Law. This Intangible Property Assignment shall be governed by and construed in accordance with the laws of the State of California.

9. Joint and Several. The respective representations, warranties, covenants, and obligations of Assignor and Assignee shall be joint and several as to each party comprising Assignor.

10. Exhibits. Exhibits A, B, C, and D attached to this Intangible Property Assignment are incorporated in this document by this reference.

11. Counterparts. This Intangible Property Assignment may be executed in any number of counterparts, all of which taken together shall constitute one and the same instrument. The signature page of this Intangible Property Assignment may be detached from and added to any counterpart of this Intangible Property Assignment identical in form.

IN WITNESS WHEREOF, Assignor and Assignee have executed this Intangible Property Assignment as of the date specified above.

Assignor: _ _[*Name of corporation*]_ _,
a _ _[*state of incorporation*]_ _ **corporation**

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

Assignee: _ _[*Name of corporation*]_ _,
a _ _[*state of incorporation*]_ _ **corporation**

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

[*ALL SIGNATURES MUST BE ACKNOWLEDGED*]

© The Regents of the University of California

Appendix K

Estoppel Certificate From Tenants

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

To: _ _[*Buyer's name and address*]_ _

The undersigned certifies that:

1. I am the tenant and present occupant of _ _[*describe legal premises*]_ _ (the Premises), _ _[*address*]_ _,

[*Add if leased premises are a portion of a larger building*]

which contains _ _[*number*]_ _ square feet of gross leasable area and which constitutes a portion of the property (the Building) located at _ _[*describe property containing the building*]_ _.

2. The Premises are leased under a lease dated _ _[*date*]_ _, _ _[*as amended by documents dated _ _[date]_ _, and _ _[date]_ _]_ _. A copy of the lease and all amendments (collectively, the Lease) are attached. The Lease contains all the agreements between me and the landlord. The Lease has not been amended or modified, either verbally or in writing, except as shown on this attachment.

3. The Lease provides for minimum monthly rent. Minimum rent of _ _[*dollar amount*]_ _ per month has been paid through _ _[*date*]_ _.

[*Choose appropriate statement*]

[*Add if lease provides for percentage rent*]

The Lease provides for percentage rent payable in the amount of _ _[*number*]_ _ percent of my gross sales in excess of _ _[*dollar amount*]_ _ per year, and percentage rent has been paid through _ _[*date*]_ _.

[*Add if tenant pays prorata share of real property taxes*]

Under the Lease, I pay a pro rata share of real property taxes. Additional charges presently payable under the terms of the Lease are _ _[*specify; if none, insert "none"*]_ _, and have been paid through _ _[*date*]_ _. I am currently paying _ _[*dollar amount*]_ _ per month for these expenses and I do not dispute landlord's method of calculation of such expenses.

[*Continue*]

I have not paid any rent in advance under the Lease except for the monthly rent that became due for the current month, and I have fully paid rent and all other amounts due under the Lease through _ _[*date*]_ _.

4. The Lease term begins on _ _[*date*]_ _, and expires on _ _[*date*]_ _ and, if the expiration date has already occurred, the Lease is now on a month-to-month basis. The Lease provides _ _[*number*]_ _ option(s) to extend or renew the lease term for _ _[*number*]_ _ years each _ _[*specify; if none, insert "none"*]_ _, and have been paid at a rental rate of _ _[*dollar amount*]_ _.

5. I have no right of first refusal or option to purchase the Premises or the Building or option to extend, option to terminate, or exclusive business rights except _ _[*specify; if none exists, insert "none"*]_ _. My only interest in the Premises or the Building is the Lease.

6. The sum of _ _[*dollar amount*]_ _ was paid to the landlord as a security deposit, and the sum of _ _[*dollar amount; if none paid, insert "none"*]_ _ was paid for the last month's rent. I shall not look to you, your successors, or assigns for the return or credit of the security deposit or any prepaid rent unless this money has been so designated and transferred to you.

7. All work required of the landlord by the Lease has been completed in accordance with the terms of the Lease, and I have accepted, and I am now in possession of, the Premises, and the Lease is in full force and effect. To the best of my knowledge: (a) the Premises comply with all applicable laws, (b) there are no hazardous materials on, in, under, or about the Premises, and (c) there are no structural or mechanical defects in the Premises. Landlord has no obligation to construct, refurbish, install, rehabilitate or renovate any existing

or additional improvements in the Premises or in the Building, except _ _[*specify*]_ _.

8. No person or firm other than myself is in possession and to the best of my knowledge no other person or firm other than the landlord has a future right to the Premises. _ _[*If anyone else has such rights, state name, address, and explain such rights.*]_ _

9. I have not assigned or entered into any subleases of the Lease, except as follows: _ _[*Specify; if no subleases exist, insert "none"*]_ _.

10. I claim no offset, counterclaims, or credits against rentals, nor do I possess or assert any claims against the landlord for any failure of performance of any of the terms of the Lease, and _ _[*add, if appropriate, "to my actual knowledge"*]_ _ the landlord is not in default under the Lease or in connection with the Premises or the Building. _ _[*If there is any claim, offset, or default, explain.*]_ _ Landlord has fulfilled all of its duties and obligations under the Lease.

11. I am not in bankruptcy, and I am not now contemplating filing bankruptcy. I have not filed and there has not been filed against me any petition in bankruptcy, voluntary or otherwise, or an assignment for the benefit of creditors, any petition seeking reorganization or arrangement under the bankruptcy laws of the United States or of any State, or any other action brought under such bankruptcy laws.

12. I have no notice of a prior assignment, hypothecation, or pledge of rents under the Lease or of the Lease.

13. On landlord's notice to me of the closing of your acquisition of the Building, I shall attorn to, be liable to, and recognize you as the landlord under the Lease, and shall be bound by and perform all of the obligations imposed by the Lease on me, and you shall succeed to all of the rights of the landlord under the Lease. However, I acknowledge and agree that you shall not be liable for any act or omission of any person or party who may have been a landlord under the Lease before your acquisition of title to the Building, and you shall not be subject to any offset or defenses which I may have against any such prior landlord.

14. On your notice of closing your acquisition of the Building, I shall make all rental and other payments and send all other notices under the Lease to you at:

_ _[*Address of buyer*]_ _

or to such other entity or address as landlord shall direct in writing.

15. The statements in this letter may be relied on by the landlord, the buyer of the Building, and any lender who extends credit in connection with the purchase of the Building. I agree that, on receipt of notice of the name and address of any lender who holds a deed of trust on the Building, I will give the lender notice of any default by the landlord during the term of the lease and a reasonable period after the default within which the lender may cure the default.

This certificate was executed on _ _[*date*]_ _.

Date: _ _ _ _ _ _ **Tenant:**

_ _[*Name of entity*]_ _,
_ _[*specify, e.g., a California corporation*]_ _

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

© The Regents of the University of California

Appendix L

Tenant Letter

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

_ _[*Date*]_ _

Re: Lease dated _ _[*date*]_ _ (Lease);

_ _[*Address*]_ _ **(the Property)**

Ladies and Gentlemen:

You are advised that, as of the date of this letter, _ _[*name of seller*]_ _ (Seller) has sold its entire interest in the referenced Property to _ _[*name of buyer*]_ _ (Buyer). In connection with the sale of the Property, Seller conveyed to Buyer all of Seller's right, title, and interest under the Lease. As of the date of this letter, Buyer has assumed all rights and obligations under the Lease. From and after the date of this letter you are advised to perform all of your duties under the Lease directly to Buyer. All rent and other payments should be made to Buyer at:

_ _[*Address*]_ _

Representatives of Buyer may be contacted by telephone at _ _[*telephone number*]_ _.

Very truly yours,

_ _[*Name of corporation*]_ _,
a _ _[*state of incorporation*]_ _ **corporation**

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

© The Regents of the University of California

Appendix M

Spousal Waiver

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

_ _[*Name of spouse*]_ _ **acknowledges that** _ _[*he/she*]_ _ **is the spouse of** _ _[*name of seller*]_ _**, who executed the attached purchase and sale agreement, and further acknowledges that the real property described in the attached agreement is seller's separate property and waives any requirement that** _ _[*he/she*]_ _ **join in the execution of any other document required for the transaction set forth in the attached agreement, and agrees to execute a quitclaim deed if necessary so that buyer can obtain title insurance.**

Date: _ _ _ _ _ _ __[*Signature of spouse*]__
_ _[*Typed name*]_ _

Comment: If the property to be sold is separate property, this form of waiver or a quitclaim deed should be obtained by the buyer.

© The Regents of the University of California

Appendix N

Alternate Natural Hazard Conditions Disclosure

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

HAZARD AREA DISCLOSURE

SELLER AND SELLER'S AGENT, IF ANY, HEREBY DISCLOSE TO BUYER THE INFORMATION CONTAINED IN THIS SECTION. SELLER ACKNOWLEDGES THAT, ALTHOUGH SUCH DISCLOSURES DO NOT CONSTITUTE WARRANTIES, BUYER SHALL HAVE THE RIGHT TO RELY ON SUCH DISCLOSURES IN DECIDING WHETHER AND ON WHAT TERMS TO PURCHASE THE PROPERTY. THE FOLLOWING DISCLOSURES ARE MADE BY SELLER AND SELLER'S AGENT, IF ANY, BASED ON THEIR KNOWLEDGE AND MAPS DRAWN BY THE STATE.

SELLER AND HIS OR HER AGENT(S) HEREBY DISCLOSE TO BUYER THAT THE PROPERTY LIES WITHIN THE FOLLOWING HAZARDOUS AREAS:

a. A SPECIAL FLOOD HAZARD AREA (any type Zone A or V) designated by the Federal Emergency Management Agency (Government Code §8589.3).

Yes ____

No ____

Do not know and information not available from local jurisdiction ____

b. AN AREA OF POTENTIAL FLOODING shown on a dam failure inundation map under Government Code §8589.4.

Yes ____

No ____

Do not know and information not available from local jurisdiction ____

c. A VERY HIGH FIRE HAZARD SEVERITY ZONE under Government Code §51178 or §51179. The owner of this property is subject to the maintenance requirements of Government Code §51182.

Yes ____

No ____

Do not know and information not available from local jurisdiction ____

d. A WILDLANDS AREA THAT MAY CONTAIN SUBSTANTIAL FOREST FIRE RISKS AND HAZARDS pursuant to Public Resources Code §4125. The owner of this property is subject to maintenance requirements of Public Resources Code §4291. Additionally, it is not the state's responsibility to provide fire protection services to any building or structure located within the wildlands unless the Department of Forestry and Fire Protection has entered into a cooperative agreement with a local agency for those purposes under Public Resources Code §4142.

Yes ____

No ____

e. AN EARTHQUAKE FAULT ZONE under Public Resources Code §2622.

Yes ____

No ____

f. A SEISMIC HAZARD ZONE under Public Resources Code §2696.

Yes (Landslide Zone) ____

Yes (Liquefaction Zone) ____

No ____

Map not yet released by state ____

WITHOUT LIMITATION, THESE HAZARDS MAY LIMIT THE PROPERTY OWNER'S ABILITY TO DEVELOP THE REAL PROPERTY, TO OBTAIN INSURANCE, OR TO RECEIVE ASSISTANCE AFTER A DISASTER.

THE MAPS ON WHICH THESE DISCLOSURES ARE BASED ESTIMATE WHERE NATURAL HAZARDS EXIST. THEY ARE NOT DEFINITIVE INDICATORS OF WHETHER OR NOT A PROPERTY WILL BE AFFECTED BY A NATURAL DISASTER. BUYER SHOULD OBTAIN PROFESSIONAL ADVICE REGARDING THESE HAZARDS AND OTHER HAZARDS THAT MAY AFFECT THE PROPERTY.

© The Regents of the University of California

Appendix O

Sample Tenancy-in-Common Agreement

John E. Gutierrez

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

TABLE OF CONTENTS

RECITALS

Article

1. DECLARATION OF INTENTION

2. TERM

3. UNDIVIDED INTERESTS

4. PROPERTY RIGHTS

- **4.1 Property Division**
- **4.2 Property Allocation**

5. GOVERNANCE

- **5.1 Membership**
- **5.2 Voting Rights**
- **5.3 Governance**

6. MAINTENANCE AND REPAIRS

- **6.1 Common Area Maintenance**
- **6.2 Limited Right of Entry**
- **6.3 Maintenance of Units**
- **6.4 Restricted Use Common Area Maintenance**
- **6.5 Alterations to Units**
- **6.6 Alterations of Common Area**

7. OPERATION AND MANAGEMENT

- **7.1 Separate Expenses**

7.2 Common Expenses

7.3 Assessments

7.4 Annual Accounting

7.5 Bank Accounts

7.6 Books of Account

8. USE RESTRICTIONS AND GUIDELINES

8.1 Plan of Development; Applicability; Effect

8.2 Association's Power

8.3 Owners' Acknowledgment

8.4 Initial Use Guidelines and Restrictions

9. INSURANCE

9.1 Scope of Insurance Coverage

9.2 Coverage Not Available

9.3 Annual Adjustment

9.4 Other Insurance

10. DAMAGE OR DESTRUCTION; CONDEMNATION

10.1 Damage or Destruction

10.2 Sale of Property

10.3 Condemnation

11. REFINANCING

11.1 Refinancing

11.2 Refinancing Expenses

11.3 Assumable Loans

12. RIGHT OF FIRST REFUSAL AS CONDITION PRECEDENT TO SALE OF OWNERSHIP INTEREST TO THIRD PERSON

12.1 Other Owners

12.2 Third Parties

12.3 Other Events Constituting Offers to Sell

12.4 Notice; Appraisal

12.5 Multiple Purchasing Orders

13. SALE OR EXCHANGE OF ENTIRE PROPERTY

13.1 Generally

13.2 Division of Proceeds on Sale

14. EFFECT OF TRANSFER

15. ENCUMBRANCE OF OWNERSHIP INTERESTS

16. DEFAULTS AND REMEDIES

16.1 Defaults

16.2 Remedies

17. RIGHT TO PURCHASE AS CONDITION PRECEDENT TO PARTITION

17.1 Offer to Nonelecting Owners

17.2 Appraisal Procedure

17.3 Binding Effect of Price Election

17.4 Payment of Purchase Price

17.5 Failure to Purchase Entire Interest

18. PROCEEDS FROM SALE OF PROPERTY

18.1 Interest

18.2 Entire Property

19. ATTORNEY FEES AND COSTS

20. GOVERNING LAW

21. AMENDMENT

22. INDEMNITY

23. NOTICES

24. DISPUTE RESOLUTION

24.1 Mediation

24.2 Arbitration

25. SEVERABILITY

26. NO WAIVER

27. RECORDATION

28. HEADINGS

29. BINDING

30. SEPARATE COUNSEL

TENANCY-IN-COMMON AGREEMENT

This TENANCY-IN-COMMON AGREEMENT (this Agreement) is made and entered into this _ _[*date*]_ _ day of _ _[*month*]_ _, 1997, by and among _ _[*name*]_ _, _ _[*name*]_ _, and _ _[*name*]_ _ (hereafter referred to individually as an Owner and collectively as the Owners).

RECITALS

A. Concurrent with this Agreement the Owners have acquired fee title to that certain real property located in the City of _ _[*name of city*]_ _, _ _[*name of county*]_ _ County, State of California, commonly known as _ _[*name*]_ _ and more particularly described in Exhibit A attached hereto and incorporated herein by this reference (the Property). The Owners intend to and shall own their respective interests in the Property as tenants-in-common.

B. The Owners intend to operate and manage the Property _ _[*primarily/exclusively*]_ _ as their individual principal residences. This Agreement is the Owners' expression of their intention to establish and impose on the Property mutually beneficial limitations, restrictions, easements, covenants, and conditions, all of which are imposed as equitable servitudes pursuant to a general plan to provide for the proper and orderly ownership, operation, and management of the Property and of their respective ownership interests therein. All of the limitations, restrictions, easements, covenants, and conditions, shall run with the land and shall be binding on the Owners and their successors and assigns, and all parties having or acquiring any right, title, or interest in or to any part of the Property.

THEREFORE, in consideration of the mutual covenants and agreements set forth below, the Owners, collectively and individually, hereby agree as follows:

1. DECLARATION OF INTENTION. The Owners hereby declare that their relationship in and to the Property is that of tenants-in-common, expressly subject, however, to the terms and conditions set forth in this Agreement. Nothing contained in this Agreement shall be deemed to constitute the Owners as partners or joint venturers or to prohibit multiple Owners of a single Interest from holding title as between themselves in any manner they elect. The Owners do not intend by this Agreement to create a "subdivision" under any state or local statutes, ordinances, or regulations or other applicable law.

2. TERM. The effectiveness of this Agreement shall commence upon the execution hereof, and shall continue for a period of forty (40) years unless sooner terminated by the consolidation of the Property's ownership in a single Owner, the mutual agreement of the Owners, or by legal partition of the Property.

3. UNDIVIDED INTERESTS. The Owners' fractional undivided interests (each an Interest) in the Property as of the date of this Agreement are as follows:

Owner(s)	Interest
_____	_____%
_____	_____%
_____	_____%

Each Owner's Interest shall remain as set forth above regardless of any improvements or additions made to the Property.

4. PROPERTY RIGHTS

4.1 Property Division. The Property consists of the underlying land and all improvements located thereon and is divided as follows:

(a) Units. Each unit (Unit) consists of the airspace bounded by and contained within the joists, studs,

and beams within the perimeter walls, floors, ceilings, windows, window frames, doors, and door frames and trim of such Unit, and includes the interior surface finishes of such components, including sheetrock, plaster, wallpaper, paint, panels, carpeting, or other finishes. Each Unit includes the utility installations located within its boundaries that exclusively serve the Owner thereof, including, without limitation: any appliances, hot water heaters, space heaters, air conditioning units, furnace, washer, dryer, cabinetry, and lighting fixtures. Bearing walls located within the interior of a Unit are Common Area, as defined below, not part of the Unit, except for the finished surfaces thereof. Fireplaces, chimneys, and flues are Common Area. A Unit does not include those areas and those things that comprise the Common Area. Each Unit includes both the portions of the building so described and the airspace so encompassed.

(b) Common Area. The remainder of the Property constitutes and shall be referred to herein as Common Area, and includes, without limitation: land; lawns, trees, shrubs, and all other landscaping; sidewalks, walkways, driveway areas, parking spaces and garages, fences, chimneys and fireplace flues, patios or decks (if any patio or deck extends out of the Unit boundary); the Property structure(s) (except for the Units); bearing walls, columns, girders, subfloors, roofs, slabs, and foundations; common stairways and hallways; reservoirs, tanks, pumps, motors, ducts, flues and chutes, and other central service equipment; conduits, pipes, plumbing, wires and other utility installations, wherever located, that service more than one Unit (except the outlets thereof when located within and servicing only a single Unit, and utility installations located entirely within a Unit, required to provide power, light, telephone, gas, water, sewerage, and drainage to only a single Unit); exterior sprinklers and sprinkler pipes, if any; and central television antenna or cable television installation, if any, all regardless as to location.

(c) Restricted Common Area. Portions of the Common Area, referred to as Restricted Common Area, are hereby allocated for the exclusive use of the Owner of the Unit to which they are either physically attached or assigned, including (a) the internal and external wiring and plumbing, pipes and conduits and utility installations designed to serve a single Unit; (b) any shutters, awnings, window boxes, doorsteps, porches and stairways connected thereto, exterior doors, door frames and hardware incident thereto, screens and windows, skylights, and other fixtures designed to serve a single Unit, but located outside the boundaries of such Unit; and (c) the yard, parking, storage or other spaces identified on the Property plan, attached hereto as Exhibit B and by this reference incorporated herein, by the number of the corresponding Unit, and all improvements therein, if any. Except as provided in this Agreement no other portion of the Common Area shall be Restricted Use Common Area.

4.2 Property Allocation. So long as an Owner is not in default under this Agreement _ _[*she/he/they*]_ _ shall have the right to exclusive use and possession for _ _[*her/his/their*]_ _ personal use of portions of the Property as follows:

Owner	Unit	Restricted Common Area
_____	_____	_____
_____	_____	_____
_____	_____	_____

The Owners shall have joint possession of all other portions of the Property. Each Owner may use the Common Area in accordance with the purposes for which it is intended without hindering the exercise of or encroaching upon the rights of any other Owners, subject to the rights of each Owner in any Restricted Use Common Area. No Owner shall have the right to exclusive possession of the Property or any part thereof except as provided in this section 4.2.

5. GOVERNANCE

5.1 Membership. The Owners shall operate, manage, and govern the Property as an unincorporated association (the association). Every Owner shall automatically be a member of the association. Any transfer of title to an Owner's Interest (except a transfer solely for security for a loan) automatically transfers the membership to the transferee. _ _[*Tenants who are delegated rights of use pursuant to section 8.4(b) below do not thereby become members, although the tenant and members of the tenant's family shall, at all times, be subject to the provisions of this Agreement.*]_ _

5.2 Voting Rights. Each Unit shall have one (1) vote in the association, regardless if multiple Owners co-own a single Interest. The vote cast by any co-Owner of an Interest shall be conclusively presumed to be the vote cast by all Owners of that Interest.

5.3 Governance. Because the Property contains only three (3) Units, there shall be no requirement for formal meetings to vote on matters before the association, except that the association shall meet annually to adopt the budget described in section 7.3 below. _ _[*Except as otherwise provided in this Agreement/All*]_ _ powers and duties exercised by the association shall be exercised by the _ _[*majority/unanimous*]_ _ consent of the voting Owners. The association may, from time to time and subject to the provisions of this Agreement, adopt and amend written rules of general application to the Property (Rules). Such Rules may concern any subject or matter and shall be binding on all Owners, their families, and tenants. Any duly adopted Rule or amendment to the Rules shall become effective either immediately following the date of its adoption or such later date as the Owners may deem appropriate. A copy of the Rules, as they may from time to time be adopted, amended, or repealed, shall be mailed or otherwise delivered to each Owner.

6. MAINTENANCE AND REPAIRS

6.1 Common Area Maintenance. The Owners or their agents shall keep and maintain the Common Area, in good condition and repair, shall provide lighting and landscaping services as needed and shall cause all other acts to be done which may be necessary to assure the maintenance of the Common Area in first class condition and repair. The Owners shall maintain all utility installations, if any, located in the Common Area, except those maintained by utility companies. The Owners shall conduct a "base line" inspection of the Common Area within thirty (30) days after the date of this Agreement and thereafter shall inspect the Property annually in connection with the preparation of the Property's operating budget to determine the need for any such maintenance and repair.

The Owners shall not be responsible for any maintenance, repairs, or replacements of the Common Area caused by the willful or negligent acts or omissions of any Owner, or such Owner's family, guests, or tenants, the cost of which is not covered by any insurance policy. If the repair is covered by any Owners' blanket insurance policy, the association shall be responsible for making the repairs, and the Owner responsible for the damage to the Property shall pay any deductible pursuant to the insurance policy and any increase in the policy premiums resulting therefrom. The maintenance, repair, or replacement of any items excluded from coverage under such blanket policy shall be the responsibility of the Owner responsible for the harm. If the responsible Owner fails to maintain, repair, or replace such excluded items, or pay any costs described in this subsection, the association or any Owner shall do the maintenance, make the repairs or replacements, or pay such costs and be entitled to immediate reimbursement for the cost thereof from the responsible Owner as provided in section 16.2 below.

6.2 Limited Right of Entry. The Owners, their agents, or any Owner may enter any Unit whenever such entry is necessary to perform any maintenance, repairs, or construction for which the Owners are responsible. Such entry shall be made with as little inconvenience to the Owner occupying such Unit as possible, and only upon at least twenty-four (24) hours' prior written notice to the Owner, except in the case of an emergency.

6.3 Maintenance of Units. Each Owner shall maintain and repair his or her Unit at his or her sole expense, including all interior _ _[*and exterior*]_ _ Unit maintenance, painting, cleaning, and repairing, including that of all interior walls, floors, ceilings, fixtures, appliances, and appurtenances therein or thereto and maintaining all utility lines, plumbing, pipes, and conduits that serve his or her Unit exclusively.

6.4 Restricted Use Common Area Maintenance. Each Owner granted the use of any Restricted Use Common Area shall keep and maintain such area in good repair and in a neat, clean orderly and attractive manner, at his or her sole expense.

6.5 Alterations to Units. An Owner may improve or alter any improvements within the interior boundaries of his or her Unit at his or her sole expense, provided such improvement or alteration (a) does not impair the structural or acoustical integrity of such Unit or any other Unit in the Property, any easement or hereditament on the Property, or the utilities or other systems servicing the Common Area or any other Unit, (b) does not involve altering any Common Area, (c) complies with all applicable laws and regulations governing the alteration or construction of residential property, and (d) obtains the written consent of _ _[*a majority of/all voting Owners*]_ _. Any Owner that alters _ _[*his/her/their*]_ _ Unit as provided in this section 6.5 shall be solely responsible for the payment of all property tax increases, and insurance policy premium increases and all other

costs for any insurance policy or policies obtained and maintained by the Owners arising from such alteration or improvement of the Owner's Unit. _ _[*No Owner who alters or improves _ _*[*his/her/their*]*_ _ Unit as provided in this section shall be entitled to an adjustment of his or her Interest, but shall be entitled to reimbursement for all documented expenditures approved by the association for such alteration or improvement in accordance with Article 18 below.*]*_ _*

6.6 Alterations of Common Area. No Owner shall, at his or her expense or otherwise, make any alterations or modifications to any Common Area improvements, or the exterior of _ _[*his/her/their*]*_ _* **Unit or any additions to such Unit that encroach into the Common Area, or _ _**[*his/her/their*]*_ _* **Restricted Common Area without the prior written consent of all voting Owners.**

7. OPERATION AND MANAGEMENT

7.1 Separate Expenses. At all times, each Owner shall be solely responsible for paying (a) all maintenance and repair costs, separately metered utilities, including, without limitation, all charges for water, gas, electricity, garbage, and telephone costs that relate exclusively to such Owner's Unit and Restricted Common Area, (b) all indebtedness secured by such Owner's Interest, and (c) all other expenses specifically described in this Agreement.

7.2 Common Expenses

(a) All expenses not separately allocated to individual Owners and their respective Unit and Restricted Common Area, as described in section 6.1 above, including, but not limited to, (a) all fire, liability, or other insurance premiums and charges relating to the Property; (b) all real and personal property taxes, assessments or other charges assessed against the Property; (c) all costs for repairs or replacement of any improvements, personal property, equipment, or fixtures that are part of the Common Area; and (d) except as provided herein, all other costs, charges, or expenses related to or incurred by the Owners with respect to the Property, shall, except as provided in section 6.5 above and unless otherwise agreed upon by all the Owners, be contributed to by each Owner in proportion to _ _[*his/her/their*]*_ _* **Interest and collected by the Owners as "Regular Assessments" as described below.**

(b) Notwithstanding any provision in this Agreement to the contrary, each Owner shall pay _ _[*his/her/their*]*_ _* **share of all payments due and to become due on all indebtedness secured by a deed of trust to the entire Property. Such payment shall be paid and collected as part of the Regular Assessments described below. Each Owner's share of the payments due and to become due on the promissory note in favor of _ _**[*name*]*_ _* **in the principal amount of _ _**[*number*]*_ _* **Thousand Dollars ($_ _ _, 000.00) secured by a deed of trust against the Property shall be as follows:**

Owner	**Owner's Debt Share**
_____	_____ %
_____	_____ %
_____	_____ %

The Owners shall review and, if necessary, revise each Owner's share of such indebtedness not less than semi-annually, to reflect each Owner's then current outstanding liability for such indebtedness.

7.3 Assessments. The Owners shall levy and collect assessments to defray all operating expenses, including all insurance premiums for coverage of the entire Property, payments on indebtedness secured by the entire Property, foreseeable expenses for the maintenance and repair of the Common Area, and reasonable reserves for the replacement of all Common Area improvements (Regular Assessments).

(a) Initial Assessments. Until January 1 of the year immediately following the Owners' execution of this Agreement, the Regular Assessments shall be the amount determined by the Owners. On or before the first business day of the first month immediately following the Owners' execution of this Agreement, the Owners shall prepare and distribute to each Owner a pro forma operating budget, estimating the total expenditures to be paid from the Property's operating account, including a reasonable reserve for contingencies and replacement of Common Area improvements for the remainder of the initial fiscal year.

(b) Subsequent Assessments. At least thirty (30) and not more than sixty (60) days prior to the beginning of the Owners' first complete fiscal year as Owners, and each fiscal year thereafter, the Owners shall estimate the total Regular Assessments for such year (including a reasonable reserve for contingencies and replacement of Common Area improvements, less any expected surplus from the prior year), and distribute a copy of a pro forma operating budget to each Owner. The Association shall assess the total of such charges to all Owners as the Regular Assessments.

(c) Regular Assessment Allocation and Payment. All Regular Assessments shall be allocated among each Unit as provided in section 7.2 above. Each Owner's Regular Assessments share shall be due on the first day of each _ _[*month/calendar quarter*]_ _. In the event an Owner fails to make his or her proportionate contribution for such Regular Assessments within five (5) days of the date such assessments are respectively due, the nondefaulting Owner(s) shall be entitled to collect a late fee equal to ten percent (10%) of such assessment in addition to invoking any of the remedies set forth in section 16.2 below.

(d) Special Assessments. Any time the Regular Assessments for any fiscal year are insufficient in amount due to extraordinary expenses not contemplated in the budget prepared for such fiscal year, then the Owners shall levy and collect a special assessment, applicable to the remainder of such year only, to defray, in whole or in part, any deficit which the Owners may incur with respect to the operation and management of the Property (Special Assessment). The Special Assessment shall be divided among, assessed against, and charged to each Owner and _ _[*his/her/their*]_ _ Unit in the same manner prescribed for the allocation of Regular Assessments as provided above. Special Assessments shall be due as a separate debt of each Owner and shall be payable in full to the association within such period as the association shall determine to be appropriate under the circumstances giving rise to the Special Assessment, subject to the subparagraph (c) above.

7.4 Annual Accounting. Within forty-five (45) days after the end of each fiscal year, the Association shall prepare and distribute to each Owner an accounting of Assessment receipts and disbursements for that fiscal year. If such accounting shows that a cash surplus exists in the operating account, the Owners shall vote as to whether to refund all or part of such surplus or as to whether such surplus shall be carried over to any future assessment periods to reduce any future Assessments.

7.5 Bank Accounts. All sums received or collected by the Owners from Assessments, together with any interest or late charges thereon, shall be promptly deposited in one or more insured checking, savings, or money market accounts opened in the names of all the Owners in a bank or savings and loan association selected by the Owners. All funds deposited in such account(s) shall be used solely for the benefit of the Property or distributed to the Owners.

Except for payments of interest on debts secured by the Property, withdrawals from any such account in excess of _ _[*amount*]_ _ Hundred Dollars ($_00.00) shall require the written consent of all Owners. In the event the Owners give such written consent, the actual withdrawals may then be made upon the designated signature of any one (1) of the Owners or such other representatives as the Owners may subsequently designate in writing. For purposes of determining whether unanimous consent for a withdrawal is required, all costs that relate to a single project must be aggregated. If the total cost of all amounts expended for such project then exceeds _ _[*amount*]_ _ Hundred Dollars ($_00.00), unanimous consent for the withdrawal shall be required.

7.6 Books of Account. At each annual meeting, the Owners shall designate one Owner among them to supervise the monthly collection of all Assessments, the deposit of such amounts to the Owners' mutual bank accounts, and the payment of Common Expenses, and to maintain the Property books and records.

8. USE GUIDELINES AND RESTRICTIONS

8.1 Plan of Development; Applicability; Effect. The Owners have created the Property as a residential development and, in furtherance of their and every other future Owners' interests, have in this Agreement established a general plan for the Property. The Property is subject to guidelines and restrictions governing land use, individual conduct, and uses of or actions upon the Property as provided in this Article 8. This Agreement and any Rules the Members may adopt in accordance with section 5.3 above, establish affirmative and negative covenants, easements, and restrictions (the Use Guidelines and Restrictions).

The Owners have prepared initial Use Guidelines and Restrictions that contain general provisions applicable to the Property, as set forth below. Based on these initial Use Guidelines and Restrictions, the association shall adopt the initial Rules, if any, at its initial organizational meeting or by the written consent of all Members.

8.2 Association's Power. The association shall implement and manage the Use Guidelines and Restrictions through the Rules that adopt, modify, cancel, limit, create exceptions to, or expand the Use Guidelines and Restrictions.

8.3 Owners' Acknowledgment. All Owners are subject to the Use Guidelines and Restrictions and are given notice that (a) their ability to use the Property or any portion thereof is limited thereby, and (b) the Owners may add, delete, modify, create exceptions to, or amend the Use Guidelines and Restrictions in accordance with section 8.2. By entering into this Agreement, each Owner acknowledges and agrees that the use and enjoyment and marketability of his or her Interest can be affected by these provisions and that the Use Guidelines and Restrictions and Rules may change from time to time.

8.4 Initial Use Guidelines and Restrictions

(a) Permitted Uses and Occupancy. The Property shall be used _ _[*exclusively/primarily*]_ _ for residential and related purposes in conformity with this Agreement and the requirements imposed by applicable zoning or other applicable laws. No Unit shall serve as the residence for or be occupied by more than _ _[*number*]_ _ (_ _) adults at any given time. This provision is not intended to prohibit occupancy by children.

(b) Right to Lease. Each Owner shall be entitled to lease _ _[*his/her/their*]_ _ exclusive occupancy area granted herein, _ _[*and to all the income derived therefrom*]_ _ provided: (i) _ _[*a majority/all*]_ _ of the nonleasing Owners shall approve a prospective tenant upon their review of and satisfaction with such tenant's standard form rental application, credit report, tax returns, and other information as the nonleasing Owners may reasonably request from the prospective tenant or leasing Owner, such approval not to be unreasonably withheld. Prior to executing a lease with such prospective tenant, the leasing-Owner shall provide the other Owners with written notice of the proposed rental or lease and the identity of the proposed tenant(s). Upon receipt of such notice, the other Owners shall have no more than 10 days to object in writing to such prospective tenant. If the nonleasing Owners fail to inform the leasing Owner of their objection to a prospective lessee and the reason for it in writing within the time provided, they shall be deemed to have consented to such lease; (ii) the lease (A) is in writing, (B) is for the leasing Owner's entire exclusive occupancy area, _ _[*(C) directs the tenant to make all rent and other payments due the landlord under such lease directly to the Owners responsible for collecting Assessments,*]_ _ and _ _[*(C)/(D)*]_ _ is made subject to this Agreement and any failure of the tenant(s) to comply with the terms of such documents shall be a default hereunder; (iii) such Owner complies with all applicable laws governing leasing of residential units; and (iv) a copy of the executed lease is provided to the Owners prior to the commencement of the lease term.

The leasing Owner or the association, as the case may be, shall comply with all applicable laws governing residential tenant evictions, and all expenses, including reasonable attorneys' fees, arising therefrom shall be borne solely by the leasing Owner either directly or as provided in section 16.2 below.

No Owner's exclusive occupancy area may be leased for any period less than _ _[*number*]_ _ _ _[*months/years*]_ _, provided, however, that so long as an Owner occupies his or her exclusive occupancy area as his or her principal residence, she or he shall be permitted to rent or lease such area for any shorter period of time while _ _[*he or she is/they are*]_ _ temporarily absent due to vacation, work-related travel, or medical or other emergency reasons. Nothing in this Agreement shall be construed to prohibit an Owner from sharing his or her exclusive occupancy area with a non-Owner roommate. Each leasing Owner shall provide his or her tenant with a current copy of this Agreement and all Rules promulgated by the Owners then in effect and shall be responsible for compliance by such tenant with all of the provisions of such documents during the tenant's occupancy and use of the Unit. Any Owner that leases or rents his or her Unit shall be responsible for the payment of all insurance policy premium increases and all other costs for any insurance policy or policies obtained and maintained by the Owners arising from such lease or rental of his or her Unit.

[*Add the following paragraph if association requires security deposit from leasing owners*]

An Owner that rents or leases _ _[*his/her/their*]_ _ exclusive use area shall deposit with the association a sum of money equal to _ _[*dollar amount*]_ _ and at all times maintain such deposit, as security for _ _[*his/her/their*]_ _ performance of all of _ _[*his/her/their*]_ _ financial obligations under this Agreement, including but not limited to the Owner's maintenance and repair obligations under Article VI above.

Notwithstanding an Owner's establishment and maintenance of such deposit, _ _[*she/he/they*]_ _ shall remain primarily responsible for the payment of all assessments and other financial obligations under this Agreement relating to such Owner and such Owner's interest; the association, in its sole discretion, may draw upon such deposit to offset any financial obligation incurred by such Owner with respect to the Property. Unless otherwise agreed upon by the Owners, all rents from a rented or leased Unit shall be credited towards and shall offset the financial contribution obligations of the Owner who could otherwise have occupied the rented unit.

[*Continue*]

(c) Common Area. The Common Area other than Restricted Use Common Areas shall be used for purposes incidental and ancillary to the use of Units. No improvement, excavation or work that in any way alters any Common Area from its existing state on the date of this Agreement shall be made or done except by the Owners.

(d) Prohibition of Noxious Activities. No illegal, noxious, or offensive activities shall be carried out or conducted upon any Unit or any Common Area, nor shall anything be done within the Property that is or could become an unreasonable annoyance or nuisance to neighboring property Owners.

(e) Garbage. No rubbish, trash, or garbage shall be allowed to accumulate outside of any Unit. Any trash that is accumulated by an Owner outside of a Unit shall be stored entirely within appropriate covered disposal containers and facilities located within designated garbage areas within the Common Area.

(f) Parking and Vehicle Restrictions. No motor vehicle shall be constructed, reconstructed, or repaired within the Property and no dilapidated or inoperable vehicle, including vehicles without a wheel(s) or an engine, shall be stored on the Property _ _[*; provided, however that the provisions of this subsection shall not apply to emergency vehicle repairs*]_ _. Automobiles, motorcycles, campers, boats, trailers, commercial vehicles, and trucks are not to be parked within the Property.

(g) Activities Affecting Insurance. Except as otherwise provided in section 8.4(b) (leasing) above, nothing shall be done or kept within any Unit or within the Common Area that will increase the rate of any insurance policy relating thereto without the prior written consent of all voting Owners, and no Owner shall permit anything to be done or kept within his or her Unit or within the Common Area that would cause any improvements on the Property to be uninsurable against loss by fire or casualty or result in the cancellation of any insurance on any Unit or any part of the Common Area.

(h) Right to Sell. Each Owner shall be entitled to sell his or her Interest upon (a) compliance with the requirements of section 10.2 and Articles 13 or 17, as the case may be, and (b) approval by _ _[*a majority/all*]_ _ of the nonselling Owners of the prospective buyer upon their review of and satisfaction with such buyer's standard form loan application, credit report, tax returns, and any information the nonselling Owners may reasonably request from the prospective buyer or selling Owner, such approval not to be unreasonably withheld.

9. INSURANCE

9.1 Scope of Insurance Coverage. The Owners shall purchase, obtain and maintain the following types of insurance:

(a) Fire and Casualty Insurance. A blanket policy or policies of fire and casualty insurance for the full replacement value of the Property and all improvements thereon. The insurance shall be kept in full force and effect at all times and the full replacement value of the insured property shall be redetermined on an annual basis. Depending on the nature of the insured property and the requirements, if any, imposed by institutional mortgagees having an interest in such property, the policy maintained pursuant to this section 9.1 shall contain _ _[*e.g., an agreed amount endorsement or its equivalent, an increased cost of construction endorsement or a contingent liability from operation of building laws endorsement or the equivalent, an extended coverage endorsement, vandalism, malicious mischief coverage, a special form endorsement and a clause to permit cash settlements for full insurable value in case of partial destruction*]_ _. The policy or policies required hereunder shall provide amounts or coverage as shall be determined by the Owners and shall name as insureds all of the Owners and their mortgagees as their respective interests may appear.

(b) Public Liability and Property Damage Insurance. A blanket policy or policies of comprehensive public liability and property damage insurance naming as parties insured all of the Owners. The policy or policies will insure each named party against any liability incident to the ownership and use of the Common Area and include, if obtainable, a cross-liability or severability of interest endorsement insuring each insured Owner against liability to each other insured Owner. The limits of such insurance shall not be less than One Million Dollars ($1,000,000) covering all claims for death, personal injury and property damage arising out of a single occurrence. Such insurance shall include coverage against water damage liability, liability for property of others, and any other liability or risk customarily covered with respect to projects similar in construction, location and use.

(c) Earthquake Insurance. A blanket policy for earthquake insurance for all Units and insurable improvements in the Property to the extent available at commercially reasonable rates.

9.2 Coverage Not Available. In the event any insurance policy, or any endorsement thereof, required by section 9.1 above, is for any reason not available, then the Owners shall obtain such other or substitute policy or endorsement as may be available which provides, as nearly as possible, the coverage described above.

9.3 Annual Adjustment. The Owners shall annually review all policies of insurance maintained by the Owners and adjusted, if necessary, to provide such coverage and protection as the Owners may deem prudent or as reasonably required by any mortgagee with a first priority lien against the entire Property.

9.4 Other Insurance. Each Owner may at his or her option and sole expense (a) insure his or her personal property and all improvements added to _ _[*his/her/their*]_ _ Unit, provided that such improvements insurance shall be limited to the type and nature of coverage commonly known as "tenant's improvements," provided further that any improvements constructed with funds derived from a mortgage on the Owner's Unit are to be covered by the insurance carried under section 9.1 so long as such insurance is maintained by the Owners; (b) obtain liability insurance for the interior of _ _[*his/her/their*]_ _ Unit; and (c) obtain loss assessment coverage to supplement loss coverage under any policy of insurance obtained by the association. _ _[*Except as provided in this section 9.4, no/No*]_ _ Owner shall separately insure his or her Unit against loss by fire or other casualty covered by any insurance carried by the Owners. If an Owner violates this provision, any diminution in insurance proceeds otherwise payable under the association's policies that results from the existence of such other insurance will be chargeable to the Owner who acquired such other insurance.

10. DAMAGE OR DESTRUCTION; CONDEMNATION

10.1 Damage or Destruction

(a) Repair or Reconstruction

(i) If any portion of the Property's improvements is damaged or destroyed by fire or other casualty, such improvements shall be repaired or reconstructed substantially in accordance with the original as-built plans and specifications, modified as may be required by, and in accordance with, all applicable building codes and regulations in force at the time of such repair or reconstruction and subject to such alterations or upgrades as may be approved by the Owners, unless the cost of repair or reconstruction is more than fifty percent (50%) of the current replacement cost of all Property improvements, available insurance proceeds are not sufficient to pay for at least eighty-five percent (85%) of the cost of such repairs or reconstruction, and _ _[*a majority of/all*]_ _ voting Owners and the holder of any first priority mortgage vote against such repair and reconstruction.

(ii) If the improvements are to be repaired or reconstructed and the cost for repair or reconstruction is in excess of twenty-five percent (25%) of the current replacement cost of all the Property improvements, the Owners shall designate a construction consultant, a general contractor, and an architect for the repair or reconstruction. All insurance proceeds, Owners' monies allocated for the repair or reconstruction, and any loan proceeds obtained by the Owners for the repair or reconstruction shall be deposited with a commercial lending institution experienced in the disbursement of construction loan funds (the depository) as selected by the Owners. Funds shall be disbursed in accordance with the normal construction loan practices of the depository that require as a minimum that the construction consultant, general contractor, and architect certify within 10 days prior to any disbursement substantially the following:

(A) that all of the work completed as of the date of such request for disbursement has been done in

compliance with the approved plans and specifications;

(B) that such disbursement request represents monies which either have been paid by or on behalf of the construction consultant, the general contractor or the architect and/or are justly due to contractors, subcontractors, materialmen, engineers, or other persons (whose name and address shall be stated) who have rendered or furnished certain services or materials for the work and giving a brief description of such services and materials and the principal subdivisions or categories thereof and the respective amounts paid or due to each of such persons in respect thereof and stating the progress of the work up to the date of such certificate;

(C) that the sum then requested to be disbursed plus all sums previously disbursed does not exceed the cost of the work insofar as actually accomplished up to the date of such certificate;

(D) that no part of the services and materials described in subsection (i) above has been or is being made the basis for the disbursement of any funds in any previous or then pending application; and

(E) that the amount held by the depository, after payment of the amount required in the pending disbursement request, will be sufficient to pay in full the costs necessary to complete the repair or reconstruction.

(iii) If the cost of repair or reconstruction is less than twenty-five percent (25%) of the current replacement cost of all the Property improvements, the Owners shall disburse the available funds for the repair and reconstruction under such procedures as the Owners deem appropriate under the circumstances.

(iv) The repair or reconstruction shall commence no later than 90 days after the date of such damage or destruction and shall be completed no later than 180 days after the commencement of reconstruction, subject to delays that are beyond the control of the party responsible for making the repairs. The Owner of any damaged or destroyed Unit immediately shall take such steps as may be reasonably necessary to secure any hazardous condition and to screen any unsightly views resulting from the damage or destruction.

(v) If the improvements are not repaired or reconstructed in accordance with the foregoing, all available insurance proceeds shall be disbursed among all Owners and their respective mortgagees in proportion to the respective fair market values of the Owners' respective Interest as of the date immediately preceding the date of damage or destruction as determined by a qualified appraiser selected by the Owners, after first applying the proceeds to the cost of mitigating hazardous conditions on the Property, making provision for the continuance of public liability insurance to protect the interests of the Owners until the Property can be sold, and complying with all other applicable requirements of governmental agencies. In the event of a failure to agree upon an appraiser, the appraiser shall be appointed by the then President of the _ _[*name*]_ _ County Bar Association.

(vi) If the Property is to be repaired or rebuilt in accordance with this Article 10 and either the damage to the Property is not covered under any insurance policy or the proceeds of any applicable insurance policy are not sufficient to pay all of the repair or rebuilding expenses, the Owners shall pay such noncovered expenses for the Common Area in proportion to their Interests, or an Owner exclusively shall pay such noncovered expenses for _ _[*his/her/their*]_ _ Unit or Restricted Common Areas, as the case may be.

10.2 Sale of Property

(a) If the failure to repair or reconstruct results in a material alteration of the use of the Property from its use immediately preceding the damage or destruction as determined by the Owners (a material alteration shall be conclusively presumed if repair or reconstruction costs exceed twenty-five percent (25%) of the current replacement cost of all Property improvements), the Property shall be sold in its entirety under such terms and conditions as the Owners deem appropriate.

(b) If the Property is sold, the sales proceeds shall be distributed to all Owners and their respective mortgagees in proportion to the fair market value of the Owners' respective Interests as of the date immediately preceding the date of damage or destruction as determined by the independent appraisal procedure described in section 17.2 below. For the purpose of effecting a sale under this section 10.2, each Owner agrees to cooperate with the other Owners to sell the entire Property for the benefit of the Owners. In the event the association fails to take the necessary steps to sell the Property as required hereunder within 60 days following the determination by the association of a material alteration, or if within 120 days following the

date of damage or destruction the association has failed to make a determination as to a material alteration, any Owner may file a partition action as to the entire Property under Civil Code §1359, or any successor statute, and the court shall order partition by sale of the entire Property and distribution of the sale proceeds as provided in Article 18 below.

(c) Notwithstanding anything herein to the contrary, any Owner shall have a right of first refusal to match the terms and conditions of any offer made to the association in the event of a sale of the Property under this section 10.2, provided this right is exercised within 10 days of receipt of notice by such Owner of the terms and conditions of any offer to the Owners. If such Owner subsequently defaults on his or her offer to purchase, he or she shall be liable to the other Owners and his or her mortgagees for any damages resulting from the default.

10.3 Condemnation. In the event of a taking by eminent domain of any part of the Common Area, the proceeds of condemnation shall be allocated between all Owners equally in accordance with section 10.1 above, except that in the event of a taking of any portion of any Restricted Common Area, the proceeds shall be allocated exclusively to the Owner to whom such Restricted Common Area has been assigned under this Agreement.

11. REFINANCING

11.1 Refinancing. The Owners agree that no debt secured by a lien against the entire Property shall be refinanced unless approved by _ _[*a majority of/all*]_ _ the voting Owners, except as provided in this Article 11. The Owners shall cooperate to achieve a refinancing or loan add-ons, as the case may be, for any of the following purposes without the Owners' prior consent:

(a) Sale of an Owner's Interest within _ _[*number*]_ _ days.

(b) To pay off and remove the lien of any existing debt secured by a lien against the entire Property that will mature within _ _[*number*]_ _ days.

(c) To reduce all the Owners' monthly payment amounts on any mortgage secured by a lien against the entire Property, provided that the terms of any refinancing loan for such purpose shall include an annual percentage interest rate not less than _ _[*number*]_ _ point(s) below the existing loan's annual percentage interest rate, a term not less than _ _[*number*]_ _ years shorter than the existing loan's term, and substantially similar other terms in all other respects.

(d) To pay off and remove the lien of any Owner's seller-financing loan secured primarily by a lien against an Owner's Interest.

Owners' cooperation shall include submitting loan applications, granting lenders' reasonable requests for access to Owners' credit information, and providing copies of Owners' tax returns and such other information as lenders may reasonably require to approve a loan.

11.2 Refinancing Expenses. Refinancing expenses shall be allocated to Owners in proportion to their then-existing debt shares as provided in section 7.2 above, except that all expenses arising from a refinancing for the sole purpose of facilitating an Owner's sale of his or her Interest shall be borne exclusively by such selling Owner.

11.3 Assumable Loans. In connection with the refinancing of any loan secured by the entire Property, the Owners shall reasonably attempt to secure a loan that allows for substitution and may be assumable by subsequent purchasers of then-existing Owners' Interests.

12. RIGHT OF FIRST REFUSAL AS CONDITION PRECEDENT TO SALE OF OWNERSHIP INTEREST TO THIRD PERSON. No Owner shall have the right to sell, exchange, or otherwise transfer _ _[*his/her/their*]_ _ Interest, or any part thereof, except upon the following terms and conditions and under the following circumstances. An Owner's interest in the Property, or any part thereof, may be sold, exchanged, gifted or otherwise transferred as follows:

12.1 Other Owners. To another Owner or Owners.

12.2 Third Parties. To any other person or party subject to the following conditions:

(a) The ownership interest in the Property or any part thereof which the Owner (the Selling Owner) intends to sell, exchange, or otherwise transfer to a third person shall first be offered in writing (such written offer shall hereafter be referred to as the Offering Notice) to all other Owners (the Remaining Owners) at the stated price or exchange value at which the Interest is proposed to be sold or exchanged to such third person and on the proposed terms thereof. The Remaining Owners, collectively and individually, shall have a period of _ _[*number*]_ _ (_ _) days after the effective date of the Offering Notice (as determined in accordance with Article 23) in which to accept or reject said offer. If more than one Remaining Owner individually elects to buy the Selling Owner's Interest as provided in this section 12.2, the Selling Owner shall have the sole discretion to sell to any such Remaining Owner. In the event the Remaining Owners, or any of them, accept the offer, the purchase price shall be paid as specified in section 18.1. If no Remaining Owner elects to purchase the Selling Owner's entire Interest, or the part thereof proposed to be sold, within the _ _[*number*]_ _ (_ _)-day period herein provided, then said interest may be sold to third parties in accordance with the provisions of section 12.2(d) below.

[*Add following paragraph if selling owner proposes to exchange interest*]

(b) In the event the Selling Owner proposes to exchange the Interest, the exchange value to be credited for such Interest, together with the identity of the other property for which it is being exchanged and the terms and conditions of such exchange shall be set forth in the Offering Notice. In the event of such exchange, the Remaining Owners, collectively and individually, shall have the right to acquire the Selling Owner's Interest in exchange for other property with a purchase price or exchange value and terms equal to that set forth in said offer. If more than one Remaining Owner individually elects to exchange for the Selling Owner's Interest as provided in this section 12.2, the Selling Owner shall have the sole discretion to exchange _ _[*his/her/their*]_ _ Interest to any Remaining Owner. No Remaining Owner shall have the right to participate in the acquisition of the other property for which the Selling Owner's Interest is being exchanged other than for the purposes of effecting the exchange. The Remaining Owners shall cooperate to effect such exchange provided that such Remaining Owners bear no additional costs or expenses in excess of the acquisition price of the Interest to be so acquired.

[*Continue*]

[(c)] If the Remaining Owners, or any of them, accepts the offer, an escrow shall be opened at a responsible escrow company of the Remaining Owner(s)' choice for processing the purchase of the Selling Owner's interest and escrow shall close within _ _[*number*]_ _ (_ _) days after the effective date of the Offering Notice (as determined in accordance with Article 23) or within the time stated for close of escrow as set forth in such third party's offer, whichever is later. The title insurance premium and all other costs and expenses of escrow shall be borne and paid for by the respective parties in accordance with the custom and practice then prevailing in the City of _ _[*name of city*]_ _, _ _[*name of county*]_ _ County.

[(d)] Unless the interest offered for sale _ _[*or exchange*]_ _ has been purchased in accordance with the terms and procedures set forth above, the Selling Owner may sell _ _[*or exchange*]_ _ his or her entire Interest to any third person or party during a 3-month period next following the expiration of the _ _[*number*]_ _ (_ _)-day period referred to in section 12.2(a) above, but not at a price lower than the proposed price or on terms, including without limitation interest rate, maturity, and payments, more favorable to the purchaser than the proposed terms set out in the Offering Notice. After the expiration of the 3-month period, no portion of the Selling Owner's interest may be sold _ _[*or exchanged*]_ _ without the interest first being reoffered to the Remaining Owners in accordance with section 12.2(a) above.

12.3 Other Events Constituting Offers to Sell. Upon the occurrence of any of the events enumerated below, such event shall be deemed to constitute an offer by the affected Owner, or his or her executor, trustee, personal representative, or successor-in-interest, as the case may be, to sell his or her Interest to the other Owners, or any of them, at a price and on terms as described in section 12.4.

(a) The death of the Owner;

(b) The voluntary or involuntary filing of a petition in bankruptcy or for the protection under similar insolvency laws or any general assignment of assets for the benefits of creditors; or

(c) The entry of a final decree of divorce or dissolution of marriage that transfers the Owner's Interest to

any person not a party to this Agreement (provided, however, that the Owner whose Interest was so transferred shall have a first option for 10 days from entry of such decree to purchase his or her former Interest, prior to the right of first refusal held by the other Owner(s) pursuant to this Article 12).

12.4 Notice; Appraisal

(a) Upon an Owner's death, his or her personal representative or successor-in-interest or, in the event of an Owner's bankruptcy or proposed court-ordered sale of his or her interest pursuant to a final decree of marital dissolution, the Owner himself or herself, shall give written notice to the Remaining Owner(s) of such Owner's demise, bankruptcy, or forced sale pursuant to a final decree of marital dissolution, as the case may be, and the Remaining Owner(s), or any of them, shall have the right to purchase the Interest at the Specified Purchase Price as defined in this subsection by giving written notice to the personal representative, successor-in-interest, Owner, or trustee in bankruptcy, as the case may be, within 30 after their receipt of the notice required by this section 12.4.

(b) The Specified Purchase Price for occurrences under section 12.3 shall be the then current fair market value of the Interest, less the amount of the Selling Owner's or deceased Owner's share of any debt secured by the Property as described in section 7.2(b) above, and the amount of any money advanced to the Selling Owner or the deceased Owner by the purchasing Owner, as provided in section 16.2 below. If the parties cannot agree on the fair market value, then within 15 days of a written demand by either party, the parties shall either: (a) jointly appoint an appraiser for the purpose of determining the fair market value or (b) failing a joint action, each separately designate an appraiser. In the latter case, within 5 days of their appointment, the designated appraisers jointly shall designate a third appraiser, whose determination of the Interest's fair market value shall be binding and conclusive. The failure of either party timely to appoint an appraiser shall be deemed an express approval of the other party's appraiser and such appraiser's appraisal shall be the fair market value. The fees of the appraiser(s) shall be treated as an item of the regular expenses and shall be paid in equal shares by the parties.

12.5 Multiple Purchasing Owners. In the event that more than one Remaining Owner exercise their rights to purchase a Selling Owner or deceased Owner's Interest under this Article 12, then the Selling Owner, or his or her executor, trustee, personal representative, or successor-in-interest, as the case may be, in his or her sole discretion may choose from among such Owners, provided that the selected Owner complies in all respects with the terms under this Article 12 for purchasing such Interest.

13. SALE OR EXCHANGE OF ENTIRE PROPERTY

13.1 Generally. Except as expressly provided herein, the entire Property, or any specific portion thereof, may be sold or exchanged only upon the written vote or consent of all the Owners. Each of the Owners hereby covenants and agrees to execute all documents, including grant deeds, as shall be required to effect any sale, refinance or exchange required hereunder or following such approval.

13.2 Division of Proceeds on Sale. The Owners agree that proceeds from any sale of the Property or any specific portion thereof shall be divided among them as specified in Article 18, below.

14. EFFECT OF TRANSFER. Upon the sale or other transfer to any person or party of any Owner's Interest, or any part thereof, as provided in this Agreement, the transferee or transferees shall become a tenant-in-common with the remaining Owners and their rights, interests, and obligations in and to the Property and the allocation of the proceeds therefrom shall be governed and determined in accordance with Article 18 below. Each Owner who acquires an Interest shall be personally liable only for obligations attributable to such Owner that become due and payable following the Owner's acquisition of the Interest, and shall not be personally liable for delinquent obligations of prior Owners unless the new Owner expressly assumes the personal liability; provided, however that the lien for such unpaid assessments shall remain, and if unpaid by the new Owner, may be foreclosed upon as provided in this Agreement.

15. ENCUMBRANCE OF OWNERSHIP INTERESTS. Each Owner covenants and agrees that he or she shall not encumber, hypothecate, mortgage, pledge, assign, or otherwise alienate for security purposes _ _[*his/her/their*]_ _ Interest without first obtaining the prior written consent of _ _[*a majority of/all*]_ _ the other Owners. Any such lien, encumbrance, mortgage, pledge, judgment, or other charge placed against the Property without such consent shall be removed from the Property by such Owner within 30 days from the date it is placed on the Property. Failure to remove the same within 30 days shall constitute a material breach of this

Agreement and the nonbreaching Owner may, at its option and at the sole cost and expense of the breaching Owner, immediately pay such monies or take such other actions as may be necessary to remove such lien or encumbrance. Any sums so paid, together with all costs incurred in removing such liens, including reasonable attorney fees, shall be regarded as a loan to the Defaulting Owner, enforceable and repayable as set forth in section 16.2, below.

16. DEFAULTS AND REMEDIES

16.1 Defaults. The following events shall be deemed a default (Default) if not cured within 7 days (except if the cure shall reasonably require more than 7 days and the defaulting Owner has commenced action to cure the default within such time) of the defaulting Owner's receipt of written notice from a nondefaulting Owner:

(a) An Owner's failure to pay in full when due _ _[*his/her/their*]_ _ share of any Regular or Special Assessments _ _[*for any 2 consecutive months or any cumulative period of 4 months*]_ _.

(b) An Owner's failure within 30 days after receipt of written demand from the Owners or any of them to remove any involuntary lien or encumbrance against the Property or to bond against such lien or encumbrance arising from action by the defaulting Owner.

(c) An Owner's willful and persistent breach of any other financial obligations under this Agreement.

16.2 Remedies. In addition to all other remedies permitted by law or under this Agreement, Owners or any Owner, as the case may be, that are in compliance with the terms and provisions of this Agreement (a Nondefaulting Owner) shall have the remedies described in this section 16.2 against an Owner who commits a Default (a Defaulting Owner). For all other violations of this Agreement, a Nondefaulting Owner shall have the remedies provided in Article 24 below.

(a) Advance of Funds by Nondefaulting Owner. The Nondefaulting Owner shall have the right, but not the obligation, to advance money owing by the Defaulting Owner. The amount of such advance shall constitute a loan to the Defaulting Owner and shall bear interest at the rate of the Bank of America NT & SA (San Francisco branch) reference rate in effect on the date of advancement plus three percent (3%), or the maximum legal rate, if less, from the date of advancement until paid in full.

(b) Assignment of _ _[*Reserve Funds/Rents, Issues, and Profits*]_ _. Any such advance shall be due and repayable upon demand of the advancing Nondefaulting Owner. Unless repaid on demand, any such advance, together with interest as set forth above, shall, at the option of the Nondefaulting Owner, be deducted and repaid from _ _[*the Defaulting Owner's contribution to the Owner's reserve account, if any, which the Defaulting Owner shall immediately restore/any rents, issues and profits of the Property, if any, otherwise distributable to the Defaulting Owner*]_ _.

(c) Security for Advances. The Nondefaulting Owners shall have a lien upon the ownership interest of the Defaulting Owner in the Property to the extent of such advances and interest; provided, however that such lien shall not be perfected and may not be foreclosed or otherwise enforced until recording of a Notice of Lien in the office of the County Recorder of _ _[*name*]_ _ County. Said notice shall state the name of the Defaulting Owner, the amount of the advance, together with the interest, costs and reasonable attorneys' fees, and a description of the property against which the lien has been assessed. Each lien shall secure interest on any unpaid advance or assessment and shall likewise secure costs of suit and reasonable attorney fees to be fixed and awarded by the court in the event any action or suit is brought to collect such charge.

(d) Subordination of Lien. The lien of each of the advances or assessments provided for under this section 16.2 shall be subordinate to the lien of any bona fide first or second mortgage(s) or first or second deed(s) of trust now or hereafter placed upon the Defaulting Owner's ownership interest subject to advances or assessments; provided, however, that such subordination shall apply only to the advances or assessments which have become due and payable prior to the sale of the Defaulting Owner's interest pursuant to a decree of foreclosure of any such mortgage or deed of trust or pursuant to a power of sale in such mortgage or deed of trust.

(e) Notice of Default. Any advance not repaid or assessment not paid within 15 days after the due date shall be deemed to be in default and shall bear interest from the due date at the rate of ten percent (10%) per

annum and the Nondefaulting Owner may bring an action at law against the Defaulting Owner, who shall be personally obligated to pay the same, or may foreclose the lien against the Defaulting Owner's ownership interest in the Property. No action shall be brought to foreclose the lien securing any advance or assessment under this section 16.2 less than 90 days following the mailing of a Notice of Lien described in section 16.2(c) above signed by the Nondefaulting Owner and recording of a copy of such notice in the Office of the Recorder of _ _[*name*]_ _ County.

17. RIGHT TO PURCHASE AS CONDITION PRECEDENT TO PARTITION. Each Owner shall retain all of his or her right as a tenant-in-common to unilaterally seek and obtain a partition and sale of the Property, and to otherwise act unilaterally with respect to his or her Interest therein except as expressly provided for in this Agreement; subject, however, to the satisfaction or waiver by the other Owners of the following conditions precedent:

17.1 Offer to Nonelecting Owners. In the event that any Owner(s) elects to have the Property partitioned and sold, such Owner(s) (the Electing Owner) shall first be required to offer to sell _ _[*his/her/their*]_ _ entire Interest in the Property to the other Owners (the Nonelecting Owner) as a condition precedent to the institution of legal action for partition and sale. Said offer shall be made in writing to all the Nonelecting Owners and shall contain the price and terms on which said Property is being offered. The Nonelecting Owners, collectively and individually, shall have _ _[*number*]_ _ (_ _) days after the effective date of said offer (as determined in accordance with Article 23) within which to elect to purchase (or acquire by exchange) the Electing Owner's interest in the Property. The election to purchase or acquire by exchange shall be delivered to the Electing Owner in writing prior to the expiration of said _ _[*number*]_ _ (_ _)-day period and said election shall specify whether the purchase price shall be at the price stated in the offer or the fair market value of the Property as determined by appraisal pursuant to section 17.2. If there are more than one offer from individual Nonelecting Owners, the Electing Owner shall have the sole discretion to accept an offer from among the Nonelecting Owners.

17.2 Appraisal Procedure. If the Nonelecting Owner chooses to purchase the interest of the Electing Owner based on appraisal, such appraisal shall be made using a single qualified M.A.I. appraiser mutually agreed upon by the parties. If the parties cannot agree on a single appraiser within 15 days of the effective date (as determined in accordance with Article 23) of the Nonelecting Owner's notice of purchase, then each party shall select one (1) appraiser so qualified within 15 days thereafter and the two (2) appraisers so selected shall then select a single appraiser (the Designated Appraiser) similarly qualified within 15 days following their designation. The Designated Appraiser shall make an independent appraisal of the fair market value of the Property within 30 days from the date of his or her appointment.

17.3 Binding Effect of Price Election. In the event that the Nonelecting Owner elects to purchase the Interest of the Electing Owner in lieu of partition at the price based on the net sales price established by appraisal, rather than that set forth in the Electing Owner's initial offer to sell, this election shall be binding regardless of whether the resulting price is greater or lesser than the initial offered price.

17.4 Payment of Purchase Price. In the event that the Nonelecting Owner elects to purchase (or acquire by exchange) an offered Interest in the Property, an escrow shall be established at any responsible title company selected by the purchaser, and escrow shall close within _ _[*number*]_ _ (_ _) days of the election of a Nonelecting Owner to purchase (or acquire by exchange) such Interest. Unless the parties otherwise agree, the purchase price for such Interest shall be paid in cash at the time of purchase. The title insurance premium and all other costs and expenses of escrow shall be borne and paid for by the respective parties in accordance with the custom and practice then prevailing in the City of _ _[*name of city*]_ _, _ _[*name of county*]_ _ County, provided that any additional costs incurred to effect an exchange shall be paid by the party on whose behalf they are incurred.

17.5 Failure to Purchase Entire Interest. If no Nonelecting Owner elects to purchase the Electing Owner's entire Interest, the Electing Owner shall then have the right to immediately and without further notice take all such steps as shall be necessary to effect a court-ordered partition and sale or exchange of the Property.

18. PROCEEDS FROM SALE OF PROPERTY

18.1 Interest. An Owner who sells _ _[*his/her/their*]_ _ Interest as provided in this Agreement, shall be entitled to all proceeds realized from such sale less (a) the balance as of the sale date of any liens or

encumbrances against or allocable to the Interest of such Owner as provided in this Agreement, the amount of such lien or encumbrance shall be paid to the association or other Owners individually, as the case may be; and (b) all expenses for inspections, repairs to the Owner's Unit and/or Restricted Common Area, refinancing or loan assumption fees, and other closing expenses arising from such sale.

18.2 Entire Property. The Owners agree that upon the sale of the entire Property, and following repayment of the outstanding principal and interest on all indebtedness secured by blanket liens on the Property, the balance of proceeds, if any, shall be divided among the Owners in proportion to their respective Interests, except that an Owner's share shall be (a) reduced by the balance as of the date of the sale of any liens or encumbrances against or allocable to the Interest of such Owner as provided in Article 16 and the amount of such lien or encumbrance shall be paid to the lienholder Owner(s) _ _[*; and (b) if the Owners' documented and approved relative expenditures for alterations or improvements to their respective Unit or Restricted Common Area as provided in Article 6 above are unequal, increased by the amount, if any, by which such Owner's approved expenditures exceed the other Owners' lowest approved expenditures for such alterations or improvements*]_ _. In addition, all other costs and expenses allocated to the Owners in connection with such sale, including, but not limited to, escrow costs, title insurance premiums, and transfer taxes, shall be divided between the Owners in proportion to their respective Interests.

19. ATTORNEY FEES AND COSTS. If any party hereto institutes any legal action or arbitration to enforce or interpret this Agreement, or for damages for any alleged breach hereof, the prevailing party in such proceeding shall be entitled to reasonable attorney fees in addition to all other recoverable costs and damages.

20. GOVERNING LAW. This Agreement shall be subject to, governed by, and construed in accordance with the laws of the State of California.

21. AMENDMENT. This Agreement may be amended in whole or in part only by mutual written agreement of all of the Owners. Any amendment of this Agreement shall be dated, acknowledged, and recorded, and shall be labeled "Amendment to Tenancy-In-Common Agreement," and if, and to the extent, any conflict arises between the provisions of any earlier document or documents, the most recent duly executed amendment shall be controlling.

22. INDEMNITY. Each Owner shall indemnify and hold harmless each of the other Owners from any and all expense and liability resulting from or arising out of any negligence or misconduct on his or her part to the extent that the amount exceeds the applicable insurance carried by the Owners on the Property.

23. NOTICES. Notices, demands, and acceptances required or permitted to be given hereunder shall be in writing and shall be sent personally delivered or by registered or certified mail, return receipt requested, postage prepaid, to the Owners' Units or such other address as an Owner may designate in writing to the other Owners. Such notice shall be deemed delivered and effective upon personal delivery or, if mailed, 48 hours after the postmark thereon.

24. DISPUTE RESOLUTION. Except as provided in Article 16 and actions for injunctive relief, to compel arbitration, or for unlawful detainer, any controversy, dispute, or claim arising out of, in connection with, or in relation to the interpretation, performance, or breach of this Agreement shall be resolved, at the request of any Owner, as follows:

24.1 Mediation. Before instituting any arbitration relating to the rights and/or duties of the Owners under this Agreement, other than the payment or collection of any assessments, the Owner that desires to initiate such action (the Complainant) must make a good faith attempt to mediate such dispute in accordance with this section. The Complainant shall send the other party(ies) (the Respondent(s)) written notice of the nature of the dispute, the facts giving rise to such claim, and the Complainant's desire to mediate the matter (the Mediation Notice). The Mediation Notice shall name a mediator (who shall have at least 3 years' experience mediating real estate disputes in _ _[*name*]_ _ County and no personal or business relationship with the Complainant). The parties shall share the cost of initiating and conducting mediation equally. Within 7 days of Respondent's receipt of the Mediation Notice, Respondent shall inform Complainant in writing if Respondent does not agree with Complainant's choice of mediator (the Rejection Notice). Such Rejection Notice shall include the name of Respondent's choice of qualified mediator as provided in this section 24.1. Complainant and Respondent's mediators shall then select a third qualified mediator to hear the dispute. Within 30 days after the final mediator is chosen, the parties shall schedule and attend a mediation session and attempt in good faith to resolve their dispute. If the mediation does not resolve the dispute or if the Respondent refuses

to attend such mediation, the Complainant may commence arbitration as provided below. The requirements of this provision shall not apply under circumstances where the Complainant would be entitled to injunctive or declaratory relief.

24.2 Arbitration. In case of any claim or dispute between Owners that relates to the rights and/or duties of the Owners under this Agreement, the dispute shall be submitted to, and conclusively determined by binding arbitration conducted by a retired judge from the panel of JAMS/Endispute, Inc., appointed pursuant to the provisions of California Code of Civil Procedure §638(1). The parties intend this general reference agreement to be specifically enforceable in accordance with said §638(1). If the parties cannot agree upon a member of the JAMS/Endispute panel, one shall be appointed by the Presiding Judge in _ _[*name*]_ _ County. The arbitrator shall award costs and attorney fees to the prevailing party _ _[*and shall have the authority to order a sale of the Property in accordance with Code of Civil Procedure §872.820 to effectuate any remedy provided in this Agreement*]_ _. The provisions of this section 24.2 shall not preclude an Owner from seeking injunctive or other provisional or equitable relief to preserve the status quo pending the parties' resolution of their dispute, and the filing of an action seeking injunctive or other provisional relief shall not be construed as a waiver of that Owner's arbitration rights.

NOTICE: BY INITIALING IN THE SPACE BELOW, YOU ARE AGREEING TO HAVE ANY DISPUTE ARISING OUT OF THE MATTERS INCLUDED IN THE "ARBITRATION" PROVISION DECIDED BY NEUTRAL ARBITRATION AS PROVIDED BY CALIFORNIA LAW AND YOU ARE GIVING UP ANY RIGHTS YOU MIGHT POSSESS TO HAVE THE DISPUTE LITIGATED IN A COURT OR JURY TRIAL. BY INITIALING IN THE SPACE BELOW, YOUR ARE GIVING UP YOUR JUDICIAL RIGHTS TO DISCOVERY AND APPEAL, UNLESS SUCH RIGHTS ARE SPECIFICALLY INCLUDED IN THE DISPUTE RESOLUTION PROVISION. IF YOU REFUSE TO SUBMIT TO ARBITRATION AFTER AGREEING TO THIS PROVISION, YOU MAY BE COMPELLED TO ARBITRATE UNDER THE AUTHORITY OF THE CALIFORNIA CODE OF CIVIL PROCEDURE. YOUR AGREEMENT TO THIS ARBITRATION PROVISION IS VOLUNTARY.

WE HAVE READ AND UNDERSTAND THE FOREGOING AND AGREE TO SUBMIT DISPUTES ARISING OUT OF THE MATTERS INCLUDED IN THE "ARBITRATION" PROVISION TO NEUTRAL ARBITRATION.

Initials: _____

_____

_____

25. SEVERABILITY. In the event any part or provision of this Agreement shall be determined to be invalid or unenforceable under the laws of the State of California, the remaining portions of this Agreement which can be separated from the invalid, unenforceable provisions shall, nevertheless, continue in full force and effect.

26. NO WAIVER. The waiver, by any party hereto, of any covenant contained herein, shall not be deemed a continuing waiver of same or of any other covenant contained herein.

27. RECORDATION. Each of the Owners agrees that a memorandum of this Agreement shall be recorded, and each of the Owners covenants and agrees to execute and acknowledge such memorandum in proper recordable form.

28. HEADINGS. The section headings herein are for convenience of reference only and shall in no way define, increase, limit or describe the scope or intent of any provision of this Agreement.

29. BINDING. This Agreement shall inure to the benefit of, and shall be binding upon, each of the Owners, their heirs, assigns, and successors-in-interest and shall constitute a covenant running with the Property.

30. SEPARATE COUNSEL. This Agreement has been drafted by _ _[*name*]_ _, Esq., as attorney for _ _[*the Owners jointly/_ _[name]_ _, individually*]_ _. The Owners acknowledge that they have been advised by _ _[*name*]_ _, Esq., of their right to consult with his or her separate legal, tax, and financial counsel about the terms of this Agreement, and have had adequate opportunity to consult with such separate counsel before signing this Agreement. _ _[*Individual representation only: Furthermore, each Owner acknowledges that he or she is relying exclusively on the advice and counsel of his or her separate legal, tax, and financial counsel in deciding to enter into this Agreement*]_ _.

IN WITNESS WHEREOF, the Owners, and each of them, have executed this Agreement on the day and year first set forth above.

OWNERS:

_____

_____

_____

Attachments:

EXHIBITS	**A**	**Property Legal Description**
	B	**Property Plan**

© The Regents of the University of California

Appendix P

Access License and Indemnity Agreement

To download **Word** version, right click and choose *Save Target As*

To download **WordPerfect** version, right click and choose *Save Target As*

Note: CEB is grateful to Sherry L. Geyer of Reed Smith LLP, San Francisco, for providing this form. The reader should carefully review and conform it to the circumstances of his or her transaction.

This Access License and Indemnity Agreement (Agreement) dated _ _[*date*]_ _, is entered into by and between _ _[*name*]_ _, a _ _[*e.g., California corporation*]_ _ (Buyer), and _ _[*name*]_ _, a _ _[*e.g., California limited liability company*]_ _ (Seller), with respect to the following facts.

RECITALS

A. Seller is the owner of that certain land and improvements located at _ _[*address*]_ _, California, more particularly described on Exhibit A hereto (the Property).

[*Add one of the following alternatives*]

[*Alternative 1: option to purchase*]

B. Buyer and Seller have entered into that certain _ _[*e.g., Option to Purchase*]_ _, dated _ _[*date*]_ _, pursuant to which Buyer may acquire the Property.

[*Alternative 2: nonbinding letter of intent*]

B. Buyer and Seller have entered into a _ _[*e.g., nonbinding letter of intent*]_ _, dated _ _[*date*]_ _, in connection with Buyer's purchase of the Property and are currently in negotiations on the terms of a purchase agreement.

[*Continue*]

C. In connection therewith, Seller has agreed to allow Buyer access to the Property and to undertake its due diligence investigation of the Property on the terms and conditions set forth in this Agreement.

AGREEMENT

NOW, THEREFORE, in consideration of the foregoing, and for other good and valuable consideration the receipt and sufficiency of which is hereby acknowledged, the parties agree as follows:

1. License. Seller hereby grants to Buyer and to Buyer's agents, engineers, contractors, consultants, representatives, and employees (collectively, Buyer's Agents) a license to enter on the Property during normal business hours for purposes of evaluating the Property and performing such investigations and studies relating to the physical and environmental condition of the Property and such other factors as Buyer deems prudent in determining whether to purchase the Property (the Due Diligence Investigation).

2. Invasive Testing; Notice of Entry. Despite the license granted above, no invasive testing, including any Phase II environmental site assessment, will be conducted without the prior written approval of Seller, which approval may be withheld in Seller's _ _[*sole/reasonable*]_ _ discretion. Before entering the Property, Buyer will deliver to Seller written (which may be by e-mail) or verbal notice at least 2 business days before its proposed entry. A representative of Seller may be present to accompany Buyer while Buyer performs any testing of the Property. All inspections and testing undertaken on the Property will be completed in a good and workmanlike manner and undertaken in a manner to cause as little damage to the Property and as little disruption to the occupants of the Property as reasonably possible.

3. Repair of Damage; Indemnity. If there is any damage to the Property caused by Buyer's or Buyer's Agents'

entry onto or testing of the Property, Buyer will restore the Property to the same condition existing before Buyer's or Buyer's Agents' entry onto the Property. Buyer will keep the Property free from all liens and will indemnify and hold Seller and Seller's officers, directors, employees, members, partners, trustees, representatives, lenders, beneficiaries, heirs, successors, and assigns harmless from and against any and all claims, demands, liabilities, judgments, penalties, losses, costs, damages, and expenses (including attorney fees) relating to or arising from Buyer's or Buyer's Agents' entry onto or testing of the Property; provided, however, that Buyer will not be liable to Seller under the foregoing indemnity as a result of the discovery by Buyer of a preexisting condition in, on, or under the Property.

4. Insurance. Buyer will maintain, and will ensure that its agents, consultants, and contractors maintain, public liability and property damage insurance insuring against any liability arising out of any entry, tests, or investigations of the Property pursuant to the provisions hereof. Such insurance maintained by Buyer or its consultants, agents, and contractors (as applicable) will be in the amount of _ _[*dollar amount*]_ _ combined single limit for injury to or death of one or more persons in an occurrence, and for damage to tangible property (including loss of use) in an occurrence. The policy maintained by Buyer will insure the contractual liability of Buyer covering the indemnities herein and will (1) name the Seller and its property manager (and their successors, assigns, and affiliates) as additional insureds, (2) contain a cross-liability provision, and (3) contain a provision that the insurance provided by Buyer hereunder will be primary and noncontributing with any other insurance available to Seller. The aforementioned insurance coverage may be obtained under a blanket policy carried by Buyer or its agents, consultants, or contractors, as the case may be. Buyer will provide Seller with evidence of such insurance coverage before any entry, tests, or investigations of the Property.

5. Manner of Giving Notice. Except as otherwise provided herein, all notices and demands that either party is required or desires to give to the other will be given in writing by personal delivery, express courier service, certified mail, return receipt requested, or by facsimile followed by next-day delivery of a hard copy to the address or facsimile number set forth below for the respective party, provided that if any party gives notice of a change of name, address, or facsimile number, notices to that party will thereafter be given as demanded in that notice. All notices and demands so given will be effective upon receipt by the party to whom notice or a demand is being given.

To Seller: _ _[*name*]_ _
_ _[*address*]_ _
_ _[*address*]_ _
_ _[*phone number*]_ _
_ _[*facsimile number*]_ _

To Buyer: _ _[*name*]_ _
_ _[*address*]_ _
_ _[*address*]_ _
_ _[*phone number*]_ _
_ _[*facsimile number*]_ _

6. Professional Fees. If either Buyer or Seller commences any action, suit, or proceeding, including arbitration, against the other party arising out of or in connection with this Agreement, the prevailing party will be entitled to recover from the other party all costs and expenses of the action, suit, proceeding, arbitration, or appeal, including reasonable attorney fees and costs, accounting and engineering fees, and any other professional fees resulting therefrom.

7. Entire Agreement. This Agreement is the final expression of, and contains the entire agreement between, the parties with respect to the subject matter hereof and supersedes all prior understandings with respect thereto. This Agreement may neither be modified, changed, supplemented, or terminated, nor may any obligations hereunder be waived, except by written instrument signed by the party to be charged or by its agent duly authorized in writing or as otherwise expressly permitted herein. Nothing in this Agreement is intended to create any agreement or obligation by either party to sell or purchase the Property (as the case may be) or, with respect to Buyer and Seller, to negotiate a definitive purchase and sale agreement between them.

8. Governing Law. The parties hereto acknowledge that this Agreement has been negotiated and entered into in the State of California. The parties hereto expressly agree that this Agreement will be governed by,

interpreted under, and construed and enforced in accordance with the laws of the State of California.

9. Authority. Each person executing this Agreement represents and warrants that he or she has the power and authority to execute and deliver this Agreement on behalf of the party for which such execution and delivery is being made.

10. Counterparts. This Agreement may be executed in any number of counterparts, each of which will be deemed an original, and all of which, together, will constitute one and the same instrument.

Buyer: _ _[*NAME OF CORPORATION*]_ _,
a _ _[*state of incorporation*]_ _ **corporation**

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

Seller: _ _[*NAME OF CORPORATION*]_ _,
a _ _[*state of incorporation*]_ _ **corporation**

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its: _ _[*Title*]_ _

Exhibit A

Legal Description of Property

© The Regents of the University of California

Appendix Q

Hotel Purchase and Sale Agreement

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

Note: This form is being provided as a sample. It has not been reviewed or edited by CEB. The reader should carefully review and conform it to the circumstances of his or her transaction. CEB is grateful to Timothy N. Brown for providing this form, which he modified from an agreement drafted by Anthony Theophilos of Starr Finley LLP in San Francisco.

This Hotel Purchase and Sale Agreement (this "Agreement") is made as of _____, 200__, (the "Effective Date") between _____, a _____ ("Seller"), and _____, a _____, or its permitted assignee ("Buyer").

RECITALS

A. Seller owns the _ _[*name*]_ _ Hotel, _ _[*address*]_ _, California, located on a parcel of land more particularly described on Exhibit A attached to this Agreement.

B. Seller wishes to sell and Buyer wishes to buy the Hotel on the terms and conditions of this agreement.

ARTICLE 1

AGREEMENT OF SALE

1.1 The Property. Subject to and on the terms and conditions of this Agreement, Seller shall sell to Buyer and Buyer shall purchase from Seller all of Seller's right, title, and interest in the Property, which shall include the Land, the Fixtures, the Improvements, the Furniture and Equipment, the Inventory, the Expendables, the Consumables, the Liquor License, the Service Contracts, the License Agreement, the Management Agreement, the Leases, the Equipment Leases, the transferable Licenses and Permits, the Reservation Deposits, the Goodwill, the Books, Records and Plans, the Advance Bookings, the Intellectual Property, and the Other Property. (Capitalized terms used in this Agreement are defined in section 11.1.)

1.2 Purchase Price. The full purchase price (the "Purchase Price) for the Property shall be _ _[*amount*]_ _ Dollars (_ _[*dollar amount*]_ _).

1.3 Deposits. The Purchase Price shall be payable as follows:

(a) Within 5 days of the Effective Date, Buyer shall deposit into an escrow (the "Escrow") established at _ _[*street and city*]_ _, _ _[*county*]_ _, California, _ _[*name of escrow holder*]_ _, ("Escrow Holder"), in cash or by certified or cashier's check made payable to Escrow Holder, the amount of _ _[*amount*]_ _ Dollars (_ _[*dollar amount*]_ _) as a deposit against the Purchase Price (the "Initial Deposit"), such Initial Deposit to be held in an interest bearing account, with interest accruing for the benefit of Buyer until Closing. Upon the delivery to Seller of the Due Diligence Approval (as such term is defined below), the Initial Deposit shall be nonrefundable except upon default by Seller hereunder or the failure of any of the conditions precedent set forth in section 6.1 below;

(b) Within 5 days of delivery to Seller of the Due Diligence Approval (as such term is defined below), Buyer shall deposit into Escrow the amount of _ _[*amount*]_ _ Dollars (_ _[*dollar amount*]_ _) (the "Second Deposit", which together with the Initial Deposit is called the "Deposit"), such Second Deposit to be held in an interest bearing account, with interest accruing for the benefit of Buyer until Closing. Upon delivery to Seller of the Due Diligence Approval, the Second Deposit shall be nonrefundable except upon default of Seller or the failure of any of the conditions precedent set forth in section 6.1 below.

(c) The balance of the Purchase Price shall be paid at Closing pursuant to Article 7 below.

1.4 Manner of Payment. Subject to the terms and conditions of this Agreement, Buyer shall pay to Seller the Second Deposit and the balance of the Purchase Price by electronic transfer of federal funds or other immediately available funds.

1.5 Allocations. Seller and Buyer hereby agree that the Purchase Price shall be allocated between the Real Property and the Personal Property by negotiation between Seller and Buyer prior to the Closing, but their failure to agree on an allocation shall not constitute a condition precedent to such Closing.

1.6 Liabilities Not Assumed. The sale of the Property shall be a transfer of assets only, and no indebtedness, accounts payable, liabilities or obligations of whatever kind or nature (including without limitation any Claims) whether actual or contingent, incurred by Seller prior to or after the Effective Date or the Closing Date, shall be assigned by Seller or assumed by Buyer, except for (i) any liabilities to provide hotel accommodations and services pursuant to confirmed reservations for periods subsequent to the Closing Date as permitted by the terms of this Agreement and (ii) those specific liabilities expressly assumed by Buyer herein.

1.7 "As Is" Sale. Buyer acknowledges and agrees that it (a) has made such investigations of the title to and physical condition of the Property and the operating history of the Property as it deems appropriate, (b) has not relied, is not relying and will not rely on any statements, representations, or projections, whether oral or written, heretofore or hereafter made by Seller or any of its officers, agents, partners, brokers or employees in connection with the physical condition of the Property, (c) is or at Closing will be fully satisfied with the business, operations and conditions of the Property, and (d) will be solely responsible for making a final inspection of the Property. Buyer acknowledges and agrees that Buyer will be consummating the purchase of the Property based solely upon Buyer's inspections and investigations of the Property and that Buyer will be purchasing the Property on an "AS IS" and "WHERE IS" basis. Without limiting the above, Buyer acknowledges that neither Seller nor its consultants, employees, or agents have made any other representations or warranties of any kind on which Buyer is relying as to any matters concerning the physical condition of the Property, including, but not limited to, the conditions and restrictions affecting the Property, water or water rights, topography, drainage, soil, subsoil of the Property, the utilities serving the Property or any zoning, environmental or building laws, rules or regulations affecting the Property, except as otherwise expressly provided in this Agreement.

ARTICLE 2

DUE DILIGENCE

2.1 Preliminary Documents. Within 5 days after the Effective Date Seller shall provide, at Seller's expense, or make available for Buyer's review (to the extent not previously provided or made available) copies of the following documents to the extent they are in Seller's possession or control (collectively, the "Preliminary Documents"):

(a) Title Report. A preliminary report dated within 30 days of the Effective Date, covering the Real Property and issued by _ _[*name of title company*]_ _ (the "Title Company"), together with a legible copy of each document, map and survey referred to therein (the "Preliminary Report");

(b) Survey. An ALTA survey of the Real Property certified by a licensed surveyor and made in accordance with the most recent "Minimum Standard Detail Requirements for ALTA/ACSM Land Title Surveys" as adopted by the American Land Title Association and National Society of Professional Surveyors and showing items _ _[*list item numbers*]_ _ from Table A thereof (the "Survey");

(c) Leases. Copies of all Leases;

(d) Agreements. Copies of all Service Contracts, the License Agreement, the Management Agreement, Equipment Leases and all other written easements, covenants, restrictions, agreements, contracts, and other documents in Seller's possession or control that affect the Property or the Hotel, including without limitation any agreements of Seller relating to the insurance, service, operation, repair, supply, advertising, promotion, sale, leasing, or management of the Property or the Hotel;

(e) Plans. Access to copies of any existing Books, Records, and Plans;

(f) Operating Statements. Copies of the most recent annual budget and copies of operating statements for the Hotel, which shall cover the following periods: (a) monthly for each calendar month of the current calendar year to date, and (b) annually for the past _ _[*e.g., 5*]_ _ calendar years _ _[*year*]_ _ to _ _[*year*]_ _;

(g) Licenses. Copies of the Liquor License and all Permits and Licenses (including without limitation building permits, certificates of completion, certificates of occupancy, and environmental permits and licenses);

(h) Insurance Policies. Copies of all liability, fire, and casualty insurance policies carried by Seller in connection with the ownership of the Property or operation of the Hotel;

(i) Employees and Employee Plans. A complete list of employees (if any), their job descriptions and salaries, together with any applicable employee pension or profit-sharing plans;

(j) Furniture and Equipment. A complete list of all Furniture and Equipment;

(k) Rent Roll. A copy of the rent roll for the Property, dated no earlier than 30 days prior to the Effective Date (the "Rent Roll")

(l) As-Built Plans. Copies of any existing as-built plans and specifications for the Property;

(m) Inventories. A copy of the latest inventory of the Inventory, Consumables, and Expendables.

(n) Escrow Balances. A statement of the balance in all escrows for Furniture and Equipment, Fixtures, and capital expenses under the Management Agreement.

(o) Bookings and Deposits. A complete list of all Advance Bookings and Reservation Deposits.

(p) Reports. Copies of any reports regarding the physical condition of the Property or any environmental reports, surveys, or studies of the Property, which are dated or were issued within the previous 5 years and are in the possession or control of Seller; and

(q) Other Documents. Access to current property tax bills, and all data, correspondence, documents, agreements, waivers, notices, applications and other records with respect to the Property and the Hotel relating to transactions with taxing authorities, governmental agencies, utilities, vendors, tenants and others with whom Buyer may be dealing from and after the Closing Date.

2.2 Approval of Preliminary Documents and Physical Condition. Buyer's obligation to close Escrow and purchase the Property is subject to the condition that Buyer in its sole and absolute discretion shall have approved or disapproved each of the Preliminary Documents (and in connection with the approval thereof shall advise Seller of those Service Contracts, if any, Buyer shall assume at Closing) and the physical condition of the Property, by written notice to Seller within 45 days after the last to occur of either the Partner Approval Date or Buyer's receipt of the last Preliminary Document (the "Due Diligence Approval"). Upon such approval and delivery to Seller of the Due Diligence Approval, the Deposit shall become nonrefundable, except upon the default by Seller hereunder or the failure of any of the conditions precedent set forth in section 6.1. If Buyer fails to so notify Seller within the 45-day period as to any or all of the Preliminary Documents or as to the physical condition of the Property, then such Preliminary Documents or physical condition shall be deemed disapproved by Buyer. If Buyer in its sole and absolute discretion shall have expressly disapproved (or is deemed to have disapproved) any Preliminary Document or the physical condition of the Property, then this Agreement shall terminate, the Deposit shall be returned to Buyer, and the parties shall be released from all further obligations to the other (excepting only the confidentiality obligation of Buyer under section 10.8 below).

ARTICLE 3

REPRESENTATIONS AND WARRANTIES

3.1 Seller's Representations and Warranties. Seller makes the following representations and warranties for the benefit of Buyer:

(a) Defects. To Seller's knowledge, the Property is free of any physical or mechanical defects, except as otherwise expressly disclosed to Buyer in writing.

(b) Ordinances. To Seller's knowledge, neither the Hotel, nor the operation thereof, violates in any way any applicable laws, ordinances, rules, regulations, judgments, orders, or covenants, conditions, and restrictions, whether federal, state, local, foreign, or private. Seller has not received any request, either formal or informal, oral or written, that Seller modify or terminate any use of the Property or the Hotel.

(c) Documents. All of the Preliminary Documents delivered to Buyer pursuant to section 2.1, and all other documents delivered to Buyer by or on behalf of Seller, are true, correct, and complete copies of what they purport to be.

(d) Condemnation. Seller has received no notice of any presently pending (and to its knowledge, there are no contemplated) special assessments or proceedings to condemn or demolish the Property or any part of it, or proceedings to declare the Property or any part of it a nuisance.

(e) Utilities. To Seller's knowledge, all water, sewer, gas, electric, telephone, and drainage facilities, and all other utilities required by law or by the normal operation of the Hotel, are adequate to service the Hotel in its present use and to permit full compliance with all requirements of law and normal usage by the Hotel's guests.

(f) Licenses and Permits. To Seller's knowledge, Seller has all licenses, permits, easements, and rights of way, including proof of dedication, building permits, and occupancy permits that are required from any governmental authority having jurisdiction over the Hotel, or from private parties, in order to continue the present use of the Hotel and ensure adequate vehicular and pedestrian access to the Hotel. Such licenses, permits, easements, and rights-of-way shall be in full force and effect as of the Closing Date.

(g) Due Authorization. This Agreement and all other documents delivered by Seller to Buyer (a) have been or will be duly authorized by the limited partners of Sellers, executed and delivered by Seller, (b) are legal, valid, and binding obligations of Seller and, with respect to those documents that are instruments of conveyance, are sufficient to convey title, and (c) are enforceable in accordance with their respective terms.

(h) Operating Statements. All operating statements furnished to Buyer in connection with or pursuant to this Agreement (a) are true and correct, (b) have been prepared in conformity with generally accepted accounting principles consistently applied, and (c) accurately reflect the financial position of the Hotel as of the respective dates thereof.

(i) Environmental Compliance. To Seller's knowledge, neither the Property nor the operation of the Hotel is in violation of any applicable building, moratorium, or environmental protection law, regulation, or ordinance.

(j) Title to the Property; Taxes. To Seller's knowledge, Seller has good and marketable title to the Property free and clear of all covenants, conditions, restrictions, easements, rights of way, liens, charges, and other matters affecting title to the Property, except as disclosed in the Preliminary Report and the Survey. To Seller's knowledge, there are no unrecorded or undisclosed legal or equitable interests in the Property owned or claimed by any person, firm, or corporation. Except as set forth in the Preliminary Report, to Seller's knowledge, there are no pending or proposed special assessments against the Property.

(k) Hazardous Wastes. To Seller's knowledge, the Property and operation of the Hotel are not in violation of any federal, state or local law, ordinance, or regulation relating to industrial hygiene or to the environmental conditions on, under, or about the Land, including but not limited to soil and groundwater conditions. To Seller's knowledge, there are no environmental, health or safety hazards arising out of Hazardous Materials on, under, or about the Land, including but not limited to soil and groundwater conditions. Neither Seller nor, to Seller's knowledge, any third party (including but not limited to Seller's predecessors in title to the Property) has used or installed any underground tank, or used, generated, manufactured, treated, stored, placed, deposited, or disposed of on, under, or about the Land or transported to or from the Hotel any flammable explosives, radioactive materials, hazardous wastes, toxic substances, or related materials ("Hazardous Materials"). For purposes of this Agreement, the term "Hazardous Materials" means substances defined as "hazardous substances, hazardous materials or toxic substances" in the Comprehensive Environmental Response, Compensation and Liability Act of 1980, as amended, 42 USC §9601*, et seq*.; the

Hazardous Materials Transportation Act, 49 USC §5101, *et seq.*; the Resource Conservation and Recovery Act, 42 USC §6901, *et seq.*; those substances defined as "hazardous wastes" or as "hazardous substances" in _ _[*cite state statutes*]_ _; and in the regulations adopted and publications promulgated pursuant to each of the aforesaid laws.

(l) Insurance and Casualties. Schedule 1 attached hereto contains a true and complete description of all insurance policies presently carried by Seller affording coverage with respect to the Hotel or the Property (the "Insurance Policies Schedule"). Seller maintains each of such policies in effect and has paid all premiums due thereon in a timely manner through the date of this Agreement. The Hotel has not been materially or adversely affected in any way as a result of fire, explosion, earthquake, accident, labor trouble, requisition or taking of property by any governmental authority, flood, rainstorm, drought, riot, act of God, or any other casualty, whether or not covered by insurance.

(m) Claims. Schedule 2 attached hereto contains a true and correct description of all pending and, to Seller's knowledge, threatened Claims against Seller (the "Claims Schedule"). There are no other pending Claims of which Seller has received notice to Seller's knowledge, and no threatened Claims against Seller in any way involving or affecting the Property or the Hotel (whether for employee or guest accidents, thefts, property damage, or otherwise). Seller will advise Buyer monthly of any claims brought against Seller prior to Closing.

(n) Equipment Leases. Schedule 3 attached hereto contains a true and complete listing of all Equipment Leases (including without limitation leases of other Personal Property) entered into by Seller with respect to the Property or Hotel, and in all instances the Seller is the lessee thereunder (the "Equipment Lease Schedule"). All Equipment Leases are in full force and effect and are valid and subsisting as of the date hereof without modification, except as described in such Schedule. Seller has received no notice of default from any party to an Equipment Lease and, to Seller's knowledge, there is no outstanding default on the part of Seller or the other party or parties to such Equipment Leases, except as set forth in such Schedule. The rents set forth in the Equipment Leases are the actual current rents payable thereunder and were actually paid for the month immediately preceding the date of this Agreement. True and complete copies of the Equipment Leases and all amendments, guaranties, and other documents relating thereto have been delivered to Buyer.

(o) Service Contracts. Schedule 4 attached hereto contains a true and correct description of the Service Contracts (the "Service Contract Schedule"). All Service Contracts, the License Agreement and the Management Agreement are in full force and effect and neither Seller nor, to Seller's knowledge, any other party thereto is in default in respect of any of the terms or provisions thereof. Except as set forth in the Service Contract Schedule, all Service Contracts are terminable by Seller on not more than 30 days' notice from Seller, and there are no disputes or disagreements pending or, to Seller's knowledge, threatened between Seller and any other party under any Service Contract, the License Agreement, or the Management Agreement, nor to Seller's knowledge is there any basis for such a dispute or disagreement. True and complete copies of the Service Contracts, the License Agreement, and the Management Agreement, and all amendments, guaranties, and other documents relating thereto have been delivered to Buyer.

(p) Authorizations. To Seller's knowledge, Schedule 5 attached hereto contains a true and complete description of all Licenses and Permits held by Seller (the "Licenses and Permits Schedule"). Seller has received no notice of any violations, except as set forth in such Schedule. Seller is not aware of any action or proceeding for the revocation of any License or Permit or any other action or proceeding before any Governmental Authority that would affect Buyer's ability to conduct the Hotel as presently conducted after the Closing. To Seller's knowledge, no License or Permit is needed other than those set forth in the License and Permit Schedule. True and complete copies of all Licenses and Permits have been delivered to Buyer.

(q) Inventory. The Inventory to be sold to Buyer under this Agreement will at Closing be owned by Seller free and clear of any lien, and shall be lawfully and validly transferable to Buyer or another designated transferee.

(r) Complete Disclosure. To Seller's knowledge, neither this Agreement nor any representation or warranty contained herein, nor any Exhibit, Schedule, certificate, document, or other instrument delivered to Buyer by or on behalf of Seller contains or will contain any untrue statement of a material fact, or omits or will omit a material fact necessary to make the statements contained herein or therein not misleading.

(s) Law and Ordinances. Except for possible noncompliance with the Americans with Disabilities Act of

1990 (ADA) (42 USC §§12101-12213), to Seller's knowledge the Property and the present use and condition thereof are not in violation of any applicable governmental law, ordinance, or regulation or deed restriction, applicable to the Property, as modified by any duly issued variances. No action or proceeding relating to the Property is pending or to Seller's knowledge threatened with respect to the Property, and no written notices of violations of such legal requirements relating to the Property have been entered or received by Seller.

(t) Advance Bookings. Schedule 6 attached hereto contains a true and correct description of all Advance Bookings (including without limitation all group bookings) as of the date specified therein for the Hotel (including, with respect to each such booking, the name of the party making the booking, the rooms booked, a summary of the services to be provided and the total amount billed or to be billed by Seller with respect to such booking) of which Seller has records or information (the "Advance Bookings Schedule"). Schedule 7 attached hereto contains a true and correct description of all Reservation Deposits and any other amounts prepaid in connection with future services to be rendered in connection with the Hotel (the "Reservation Deposit Schedule").

(u) Contract Rooms. Except as set forth in Schedule 8 (the "Contract Rooms Schedule"), there are no contract room arrangements in effect at the Hotel.

(v) Furniture and Equipment. Schedule 9 attached hereto contains a true and complete description of all Furniture and Equipment (the "Furniture and Equipment Schedule").

(w) Leases. Schedule 10 attached hereto contains a true and complete description of all Leases affecting the Property or to which the Property is subject (the "Lease Schedule"). Seller is not party to any leases, occupancies, concessions, or tenancies except for the Leases, and there are no amendments or written or oral promises or understandings, agreements, or commitments between Seller and any tenant other than as set forth in the Leases. The Leases are in full force and effect, no rent has been paid in advance except for the current period or as otherwise set forth in the Leases, and to Seller's knowledge there are no defenses, setoffs, or counterclaims for the benefit of the tenants thereunder, except as disclosed in the Leases. No breach of a Lease has been committed by Seller and Seller has not received or given notice of default under a Lease that has not been cured.

3.2 Buyer's Representations and Warranties

(a) Due Authorization. Buyer represents and warrants that this Agreement (i) has been duly executed and delivered by Buyer, (ii) is a legal, valid, and binding obligation of Buyer, and (iii) is enforceable in accordance with its respective terms.

(b) Financial Resources. As of the expiration of the Due Diligence Period, Buyer will have funds available to it sufficient to consummate the transactions contemplated by this Agreement.

3.3 Effect of Representations and Warranties. Each representation and warranty in section 3.1 (a) shall survive the Closing Date pursuant to section 3.4 below and not merge with the delivery to Buyer of the Deed; (b) is material and being relied upon by Buyer; (c) is true in all respects as of the Effective date; and (d) shall be true in all respects on the Closing Date.

3.4 Survival. Each and every representation and warranty set forth in this Article 3 or any other representation, warranty, or indemnity set forth in this Agreement above shall survive the Closing for a period of 2 years thereafter.

3.5 Aggregate Liability. Seller's aggregate liability for breach of any representation or warranty set forth in this Article 3 shall in no event exceed _ _[*dollar amount*]_ _.

ARTICLE 4

COVENANTS

4.1 Seller's Pre-Closing Covenants. During the Transition Period, and except as otherwise consented to or approved by Buyer in writing and as contemplated by this Agreement, Seller will:

(a) Operation of Hotel. Operate the Hotel consistent with current practice and will use reasonable best

efforts to (i) cooperate with Buyer to preserve present relationships with suppliers, customers, employees, and other persons having business dealings with Seller, (ii) maintain present hours of operation, (iii) maintain the Hotel's good reputation, (iv) maintain in full force and effect all extended coverage, fire, casualty, public liability, and fidelity policies now in effect with respect to the Property and the Hotel, and (v) take all necessary actions to comply with all closing conditions set forth in Articles 6 and 7 for which Seller is responsible and to make all deliveries at Closing and do nothing that may hinder or delay such Closing.

(b) Maintenance. Maintain the Property, including all systems used or needed for the operation of the Hotel, in substantially the same operating condition and repair as on the Effective Date of this Agreement, continue normal operation of the Hotel and continue normal practice with respect to normal maintenance and repairs so that the Property will, except for normal wear and tear, be of at least the same quality and quantity on the Closing Date as it was on the Effective Date and, without limiting the foregoing, maintain the quantity and quality of Personal Property at approximately the current levels.

(c) No Transfer. Not sell, transfer, assign, or dispose of any of the Property (other than in the ordinary course of the operation of the Hotel) or enter into any tenant lease between the Effective Date and the Closing Date without Buyer's prior written approval, which approval shall not be unreasonably withheld or delayed.

(d) Commitments. With respect to the Property and the operation of the Hotel:

(i) Not (a) modify, extend, renew, cancel, terminate, rescind, or surrender the Management Agreement, the License Agreement, any Equipment Lease, employment contracts, Union Contract, or Employee Plans, (b) reduce any Security Deposit or Reservation Deposit, (c) permit any rental space that is now vacant or becomes vacant to be occupied, or (d) make any sale, transfer, assignment, or other disposition of any right or privilege accruing to Seller; provided, however, that Seller shall prior to Closing terminate all Service Contracts other than those identified on the Service Contract Schedule.

(ii) Not make or enter into any contract or arrangement, including any series of related contracts, concerning the purchase of Inventory, Expendables, Consumables, or Furniture and Equipment, or the maintenance and operation of the Hotel, that involves receipts, expenditures, or the provision of services with a value of more than $10,000 after Closing in the aggregate, without the prior consent of Buyer, which consent shall not be unreasonably withheld and which shall be given or withheld within 5 days after request.

(iii) Not consent to any zoning changes, or sell, transfer, assign, dispose of, or consent to the utilization of, any development rights, including air rights, if any, for the Property, or modify or amend or consent to any modification or amendment of the certificate of occupancy for the Hotel, not in the ordinary course of business.

(iv) Not make or enter into any rate agreements not in the ordinary course of business without prior notification to Buyer.

(e) Books. Maintain the books and records of the Hotel in the usual and ordinary manner, on a basis consistent with prior years, and endeavor to comply with all governmental laws, ordinances and regulations applicable to Seller, the Property, and the conduct of the operation of the Hotel, and perform all of Seller's obligations without default.

(f) Information. Furnish Buyer, within 3 days after Buyer notifies Seller of the Closing Date pursuant to section 7.1 of this Agreement, with the following:

(i) Seller's most recent operating and financial statements regarding the operation of the Hotel and lists of accounts receivable in each case when the same are prepared (and keep Buyer informed upon inquiry on a reasonable basis as to the Hotel's business operations);

(ii) a statement in writing of any fact that, if existing or known on the date of this Agreement, would have been required to be set forth in or disclosed under this Agreement;

(iii) updates for all Schedules attached to this Agreement bringing current the information provided in the Schedules; provided, however, that nothing contained in this section shall permit Seller to enter into any agreement, take any action, or incur any liability except as permitted by the provisions of this Agreement;

(iv) a list of deposits and advance payments made by Seller prior to the Closing Date with respect to Property that will be received after the Closing Date; and

(v) all such additional information relating to the Property and the Hotel as Buyer may reasonably request.

(g) Liens. Not create any Liens on the Property other than the Permitted Exceptions.

(h) Alterations. Not undertake or commence any renovations of or alterations to the Hotel or any part of it other than those already in process or within the current year's budget (a copy of which shall be provided to Buyer as a Preliminary Document), and other than those necessary to cure governmental violations or necessary to comply with requirements of governmental authorities and boards of insurance underwriters.

(i) Defaults and Permits. Not knowingly perform any act or omit to perform any act, or knowingly permit any act or omission to act, that will cause a breach or default of any of Seller's contracts, commitments, or obligations, including without limitation the Leases, the License Agreement, or the Management Agreement.

(j) Reservations Before Closing. Cause Manager under the Management Agreement to continue to solicit and accept reservations for the Hotel, including reservations for any period after the Closing Date. Seller's employees or agents located at the Hotel (if any) shall continue their usual sales and advertising programs and campaigns to solicit such reservations. Until the Closing, Seller's employees and agents located at the Hotel have used and shall continue to use their best efforts to obtain Advance Bookings and shall not book into any hotel owned or operated by Seller or its affiliates any such business that has historically been booked as part of the Hotel.

(k) Marketing. Seller's employees and agents located at the Hotel (if any) shall continue actively and diligently to market and promote the Hotel, and Seller shall consult and cooperate with Buyer in connection with marketing and sale promotions.

(l) Seller Indemnification Re Pre-Closing Acts. Seller agrees to indemnify, defend, and hold Buyer, its partners, affiliates, representatives, and agents harmless from any and all liabilities, costs, damages, claims, suits, judgments or expenses, including without limitation reasonable attorney fees, incurred by Buyer, arising out of or connected with (a) Seller's failure to perform under all of the contracts, leases, and agreements of Seller assumed by Buyer, and (b) any act or omission of Seller in connection with the ownership or operation of the Property or the Hotel prior to the Closing Date that may result in liability of Seller to any third party.

(m) Shadow Management. During the Transition Period, permit Buyer to establish a "shadow management" operation with respect to the Hotel. Buyer's personnel, agents, and representatives will have reasonable access during normal business hours to all books, records, and other information in the possession or control of Seller, Manager, or Seller's agents concerning the Hotel, and will have the right (at Buyer's expense) to establish duplicate books and records (whether in tangible or electronic form) in order to effect a smooth transition in the ownership and management of the Hotel. Buyer agrees that its shadow management personnel, agents, and representatives will not unreasonably interfere with the normal management and operation of the Hotel, will have no authority over the management and operations of the Hotel, and will not be deemed to have assumed management responsibilities before Closing by virtue of such shadow management.

(n) Cease Marketing of the Property. Not actively market the Property for sale or other accept or submit to its partners for approval offers from others prior to the Partner Approval Date, and not actively market the Property thereafter (although consideration of unsolicited offers shall be permitted after the Partner Approval Date).

4.2 Buyer's Covenants

(a) Indemnity. Buyer agrees to indemnify, defend, and hold Seller, its partners, affiliates, representatives, and agents harmless from any and all liabilities, costs, damages, claims, suits, judgments, or expenses, including without limitation reasonable attorney fees, incurred by Seller, arising out of or connected with (i) Buyer's failure to perform under all of the contracts, leases, and agreements of Seller assumed by Buyer, and (ii) any act or omission of Buyer in connection with the ownership or operation of the Property or the Hotel from and after the Closing Date.

4.3 Closing Obligations. Buyer shall take all necessary actions to comply with all closing conditions set forth in Articles 6 and 7 for which Buyer is responsible and to make all deliveries at Closing and to do nothing that may hinder or delay such Closing.

ARTICLE 5

EMPLOYEES

5.1 Employees. Buyer understands that Seller has no employees, and that _ _[*name of manager*]_ _ manages the Hotel and employs all of the employees involved in the management and operation of the Hotel, and that Seller's representations and warranties herein with respect to employees do not relate to the employees of _ _[*name of manager*]_ _.

5.2 Representation and Warranty. Seller represents and warrants that there are no other employees employed by Seller except as set forth in the Schedule 11 attached hereto (the "Employee Schedule"). Seller shall provide any updated versions of the Employee Schedule to Buyer at least monthly from the date of this Agreement and on the Closing Date.

5.3 Contracts; Labor Unions

(a) With respect to the Hotel and the operation of it, Seller represents and warrants that Seller is not a party or subject to:

(i) any employment or consulting contract or arrangement that is not by its terms terminable at will without penalty to Seller;

(ii) any plan, contract, or arrangement for bonuses or incentive compensation, deferred compensation, retirement payments, or other compensation arrangement for employees or former employees or their survivors, dependents, and beneficiaries;

(iii) any plan, contract, or arrangement not otherwise disclosed providing for any employee benefit plan, whether or not insured, for any officer or employee or former officer or employee, or their survivors, dependents, and beneficiaries; or

(iv) any Union Contract or other contract or arrangement with any labor union or trade association.

With respect to those employees identified in the Employee Schedule (if any), Seller shall not enter into any of the above before the Closing without the prior consent of Buyer.

(b) To Seller's knowledge, with respect to the employees identified in the Employee Schedule (if any), no movement to designate a collective bargaining representative for any of such employees exists or is threatened and Seller shall notify Buyer immediately if Seller learns of any such movement.

5.4 Labor Disputes. To Seller's knowledge, there are no pending or threatened grievances, arbitrations, employment discrimination or wrongful termination charges, claims, proceedings, or investigation, or other labor disputes involving employees of Seller or the Hotel that affect the Hotel or the business thereof.

5.5 Employee Plans and Benefit Arrangements; ERISA

(a) Seller does not maintain or otherwise contribute to any "employee benefit plan", as defined in §3(3) of ERISA and subject to Title IV of ERISA, that covers any employee or former employee of Seller (an "Employee Plan").

(b) Seller does not maintain any form of current or deferred compensation, bonus, benefit, welfare, or similar plan or arrangement, whether or not funded, for the benefit of any single employee or former employee or any class or classes of employees or former employees of Seller. Seller does not provide directly or indirectly group medical benefits for its former employees except benefits, if any, provided pursuant to the provisions of the federal Consolidated Omnibus Budget Reconciliation Act of 1985 ("COBRA") (29 USC §§1161-1169).

(c) Neither Seller nor any of its directors or officers nor any of their respective employees or agents, nor any "party in interest" or "disqualified person", as such terms are defined in §3 of ERISA and §4975 of the Code has, with respect to any Employee Plan, engaged in or been a party to any "prohibited transaction", as such term is defined in §4975 of the Code or §406 of ERISA, in connection with which Seller or any of its partners or their respective directors or employees or any Employee Plans or related funding medium could be subject to any liability under Title I of ERISA or a tax imposed by §4975 of the Code.

(d) No Employee Plan has been terminated and Seller does not expect any such Employee Plan to be terminated within the meaning of Title IV of ERISA; with respect to any Employee Plan that is a "multi-employer plan" as defined in §4001(a)(3) of ERISA, Seller has not incurred nor does it expect to incur any withdrawal liability under Title IV of ERISA and no such plan is in reorganization status as defined in §4241 of ERISA; with respect to any Employee Plan which is described in §413(c) of the Code, Seller has not incurred nor does it expect to incur any liability pursuant to Title IV of ERISA. Seller is not a "substantial employer" as defined in §4001(a)(2) of ERISA with respect to any Employee Plan, except as identified in Schedule 13 (the "Employee Plans Schedule") attached hereto, nor has any Employee Plan subject to Part 3 of Subtitle B of Title I of ERISA or §412 of the Code, or both, incurred any "accumulated funding deficiency" (as defined in ERISA), whether or not waived; Seller has not failed to make any contributions or pay any amounts due and owing as required by the terms of any Employee Plan; nor has there been any "reportable event" within the meaning of §§4043(b), 4062(e), 4063(a) or 4041(f) of ERISA with respect to any Employee Plan (other than the transactions contemplated by this Agreement).

5.6 Termination of Employment. Effective at Closing, Seller must terminate all employees listed on the Employee Schedule (if any), without liability to Buyer. Seller will provide Buyer with evidence reasonably satisfactory to Buyer of such terminations at Closing. Seller must comply with all notices and other requirements and obligations, if any, required by federal and state "plant closing" laws and other applicable laws and regulations, including without limitation the federal Workers Adjustment and Retraining Notification Act (the "WARN Act"), California Labor Code §§1400-1408, and any similar laws or regulations applicable to this Agreement and the transactions contemplated under this Agreement, at its sole cost and expense. With respect to all such terminated employees, Seller must comply with and pay all costs and expenses of accrued but unpaid or unearned salary, vacation pay, sick leave, pension benefits, health benefits, and all other employee benefits, and continuation of health and other benefits after termination of employment, including without limitation those under COBRA and California Health and Safety Code §§1366.20-1366.29.

5.7 Employment by Buyer. Buyer may, but will not be obligated to, offer employment to any or all of the employees on the Employee Schedule at any time. During the Transition Period, Buyer will have the right to interview applicants for employment, which may include employees listed on the Employee Schedule, and which interview process may include drug testing. Seller will provide Buyer, at no charge, with meeting facilities reasonably satisfactory to Buyer so that Buyer may engage in these interviews. Before Closing, Buyer will extend offers of employment to the employees listed on the Employee Schedule (if any) whom Buyer has elected to employ on terms and conditions satisfactory to Buyer.

5.8 No Offers of Employment. Seller and its affiliates will not offer alternative employment to any employee of Seller identified in the Employee Schedule, provided that at least _ _[*e.g., 5*]_ _ days before Closing Buyer will specify those employees of Seller to whom Buyer does not wish to make offers of employment, and, with respect to those employees to whom Buyer does not offer employment, Seller then may make offers of employment to those employees. Seller at no time will make any offers of employment to those employees to whom Buyer has made offers.

5.9 Compensation. Except with Buyer's prior written consent, (a) no increase will be made in the compensation or rate of compensation that is or will become payable to any employees of Seller or, during any period of employment at the Hotel, to employees of Seller identified in the Employee Schedule, and (b) except to the extent that Seller is presently contractually obligated to do so, no bonus, profit-sharing, retirement, insurance, death, fringe benefits, or other extraordinary compensation shall accrue, be set aside, or be paid to any officer or employee of Seller.

5.10 Indemnification. In addition to all other indemnification obligations of Seller under this Agreement, Seller must defend, indemnify, and hold harmless Buyer and its officers, directors, employees, shareholders, and affiliates from any and all claims, damages, causes of action, and liabilities (including attorney fees, costs, and expenses), with counsel reasonably acceptable to Buyer, arising out of Seller's failure to comply with the provisions of this Article or the termination of Seller's employees as provided in this Article.

ARTICLE 6

CONDITIONS PRECEDENT

6.1 Buyer's Closing Conditions. All obligations of Buyer under this Agreement are subject to the fulfillment, prior to or at the Closing, of each of the following general conditions, except to the extent otherwise waived by Buyer in writing:

(a) Approval of Preliminary Documents and Physical Condition. Buyer shall have approved each of the Preliminary Documents and the physical condition of the Property pursuant to section 2.2.

(b) Representations, Warranties, and Covenants. The representations and warranties of Seller contained in this Agreement shall be true in all material respects on and as of the Closing Date with the same effect as if such representations and warranties had been made on and as of the Closing Date. Seller shall have performed and complied in all material respects with all covenants, agreements, and conditions required by this Agreement to be performed or complied with by it prior to or on the Closing Date. Buyer shall have been furnished with a certificate of Seller dated the Closing Date, certifying to the fulfillment of the foregoing conditions, which certificate shall have the effect of a representation and warranty of Seller made on and as of the Closing Date.

(c) Title. On the Closing Date, the Title Company shall deliver to Buyer an ALTA 2006 Extended Coverage Owner's Policy of Title Insurance (including such endorsements as Buyer shall confirm are available from the Title Company during the Due Diligence Period) in the amount of the Purchase Price allocated to the Real Property and Improvements pursuant to section 1.5, including such coinsurance and/or reinsurance (with direct access) as may be required by Buyer, showing fee title to the Real Property vested in Buyer (the "Title Policy"), subject to no exceptions other than (a) a lien for local real estate taxes and assessments not yet due or payable; and (b) those exceptions appearing on the Preliminary Report and Survey and as approved by Buyer (and which Seller has agreed to remove) prior to delivery of the Due Diligence Approval (all of which foregoing exceptions shall be referred to collectively as the "Permitted Exceptions").

(d) License Agreement

(i) Buyer must have been approved by _ _[*name of hotel operator*]_ _ to operate the Hotel as a _ _[*name of hotel*]_ _ under the License Agreement and on such other terms and conditions satisfactory to Buyer in its reasonable discretion (including any property improvement program required by _ _[*name of hotel operator*]_ _ in connection with the Hotel).

(ii) At least _ _[*e.g., 10*]_ _ days before the Closing Date, Seller will furnish to Buyer an estoppel certificate from _ _[*name of hotel operator*]_ _ in the form of the attached Exhibit B ("License Agreement Estoppel Certificate"), dated no earlier than _ _[*e.g., 20*]_ _ days before the Closing Date. Buyer will have through the _ _[*e.g., fifth*]_ _ day before the Closing Date to disapprove the License Agreement Estoppel Certificate.

(iii) At least _ _[*e.g., 10*]_ _ days before the Closing Date, Seller will furnish to Buyer a subordination and nondisturbance agreement executed by _ _[*name of hotel operator*]_ _ in a form reasonably acceptable to Buyer and its lender (License Agreement SNDA), dated no earlier than _ _[*e.g., 20*]_ _days before the Closing Date.

(e) Management Agreement

(i) At least _ _[*e.g., 10*]_ _ days before the Closing Date, Seller will furnish to Buyer an estoppel certificate from _ _[*name of Manager*]_ _ in the form of the attached Exhibit C ("Management Agreement Estoppel Certificate"), dated no earlier than _ _[*e.g., 20*]_ _ days before the Closing Date. Buyer will have through the _ _[*e.g., fifth*]_ _ day before the Closing Date to disapprove the Management Agreement Estoppel Certificate.

(ii) At least _ _[*e.g., 10*]_ _ days before the Closing Date, Seller will furnish to Buyer a subordination and nondisturbance agreement executed by _ _[*name of hotel operator*]_ _ in a form reasonably acceptable to Buyer and its lender (License Agreement SNDA), dated no earlier than _ _[*e.g., 20*]_ _ days before the Closing Date.

(f) Assignments. Before the Closing, Seller must have deposited into Escrow the Assignment of License Agreement duly executed by _ _[*name of hotel operator*]_ _ and the Assignment of Management Agreement duly executed by _ _[*name of Manager*]_ _.

(g) Liquor License. As of the close of Escrow, the Liquor License must have been transferred to Buyer.

(h) Tenant Estoppels. Unless waived by Buyer or its lender, at least 10 days prior to the Closing Date, Seller shall deliver to Buyer an updated Rent Roll dated not earlier than 30 days prior to the Closing Date (the "Updated Rent Roll") and in connection therewith shall furnish a copy of a tenant estoppel certificate from each tenant or concessionaire under the Leases in the form of the attached Exhibit D (the "Tenant Estoppel Certificates"), dated no earlier than 20 days prior to the Closing Date. Buyer shall have through the fifth (5th) day prior to the Closing Date to disapprove the Tenant Estoppel Certificates.

(i) Labor Disputes. There will be no strikes, labor disputes, work stoppages, grievances, arbitrations, unfair labor practices, employment discrimination, wrongful termination charges, claims or proceedings, or other labor disputes pending or threatened in writing that would affect the intended operation of the Hotel.

(j) Consents. All governmental and third party consents in connection with the transactions contemplated by this Agreement must have been obtained and all applicable waiting periods must have expired, including the consent of _ _[*name of hotel operator*]_ _ and _ _[*name of manager*]_ _ to the assignment of the License Agreement and the Management Agreement, respectively, and their execution of the Assignment of License Agreement and Assignment of Management Agreement, respectively.

(k) Bulk Sales. Seller will deliver evidence of its compliance with all requirements, if any, of the bulk sales laws of the State of California as set forth in California Com C §§6101-6111 (Bulk Sales Laws) applicable to this transaction.

(l) No Material Adverse Changes. During the Transition Period there will not have been any event, circumstance, or breach of this Agreement that, individually or in the aggregate, will have a material adverse change or effect on the results of income, operations, or value of the Hotel and its business, taken as a whole.

(m) Litigation. Other than claims disclosed on Schedule 12 (the "Litigation Schedule"), there shall be no claims or other private or governmental litigation by any governmental authority or person pending or threatened in writing against Seller relating to the Hotel or the Property that might, if they were adversely determined, result in a material adverse change in the Property or the operations of the Hotel (or prospects for the Hotel) or that challenge the validity of or otherwise materially adversely affect the transactions contemplated by this Agreement.

(n) Liens. Buyer shall have received a report, reasonably satisfactory to Buyer and Buyer's counsel, from the Title Company or a reputable lien search company indicating that, with respect to the Property: (i) such company has reviewed appropriate recording files of financing statements, conditional sales contracts, chattel mortgages, lease agreements, notices of assignment of accounts receivable, factors, liens, trust receipts, and federal and state tax liens, and (ii) that there are no liens (including Uniform Commercial Code financing statements) of record as of a date not more than 5 days before the Closing Date with respect to the Property, other than those that will be discharged at the Closing.

(o) Closing Documents. Seller shall be ready, willing, and able to deliver each of the documents and other items it is required under this Agreement to deliver at the Closing and shall do so at the Closing.

(p) Physical Condition. The physical condition of the Property shall be substantially the same on the Closing Date as on the Effective Date, reasonable wear and tear excepted.

(q) Legal Opinion. Buyer shall have received either (i) from legal counsel to Seller an opinion in form and substance reasonably satisfactory to Buyer, opining as to the due authorization by Seller and its limited partners of the transaction contemplated by this Agreement, dated the Closing Date (the "Legal Opinion"); or (ii) from Seller a copy of Seller's limited partnership agreement and an original partnership authorization, dated the Partner Authorization Date and authorizing the sale of the Hotel by Seller pursuant to this Agreement, executed by the partners thereof required for due authorization by the express terms of the limited partnership agreement and in form and substance reasonably satisfactory to Buyer (the "Seller Authorization").

(r) Consents. All governmental and third party consents in connection with the transactions contemplated by this Agreement shall have been obtained and all applicable waiting periods shall have expired, including, without limitation, the consent of _ _[*name of licensor/franchisor*]_ _ and _ _[*name of manager*]_ _ to the assignment of the License Agreement and the Management Agreement, respectively, and their execution of the Assignment of License Agreement and Assignment of Management Agreement, respectively.

(s) Seller's Covenants. Seller shall have fully performed and complied in all material respects with its obligations, covenants and agreements under this Agreement, including without limitation those in section 4.1 above.

(t) Additional Documents. All actions, proceedings, instruments, and documents required to carry out the transactions contemplated by this Agreement or incidental to it, and all other related legal matters, shall have been completed or delivered, as the case may be, to the satisfaction of Buyer.

6.2 Seller's Closing Conditions. All of the obligations of Seller under this Agreement are subject to the fulfillment, at or prior to Closing, of each of the following conditions, except to the extent waived in writing by Seller.

(a) Representations and Warranties. The representations and warranties of Seller contained in this Agreement shall be true in all material respects on the date hereof and as of the Closing Date and shall have the same effect as if such representations and warranties had been made as of the Closing Date. Buyer shall have performed and complied in all material respects with all covenants, agreements, and conditions required by this Agreement to be performed or complied with by Buyer prior to the Closing Date.

(b) Closing Documents. Buyer shall be ready, willing, and able to deliver each of the documents and other items it is required hereunder to deliver at the Closing and shall do so at the Closing.

(c) Consents. All governmental and third party consents in connection with the transactions contemplated by this Agreement shall have been obtained and all applicable waiting periods shall have expired, including, without limitation, the consent of _ _[*name of licensor/franchisor*]_ _ and _ _[*name of manager*]_ _ to the assignment of the License Agreement and the Management Agreement, respectively, and their execution of the Assignment of License Agreement and Assignment of Management Agreement, respectively, and release of Seller from its obligations thereunder.

(d) Partner Approval. The partners of Seller shall have approved the sale of the Property pursuant to this Agreement within 3 weeks of the Effective Date (the "Partner Approval Date"). This condition shall be deemed waived unless Seller shall have notified Buyer prior to the Partner Approval Date that such approval has not been obtained, in which case this Agreement shall immediately terminate and the Deposit shall be promptly returned to Buyer, whereupon the parties shall have no further obligations hereunder (excepting only the confidentiality obligations of Buyer under section 10.8.

6.3 Hart-Scott-Rodino Act. This Agreement is subject to the condition that compliance with the reporting requirements of the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (15 USC §18a) is either (a) not required, or (b) required, and the necessary filing is completed with no objections being received under the Act. If either party determines that this transaction is subject to the Act's reporting requirements, then each party will use its best efforts to expeditiously file a completed notification report under the Act and take all other actions necessary or advisable to comply with the Act and the rules and regulations promulgated under the Act. If such requirements or such other matter as may be required by any governmental agency having jurisdiction under the Act have been complied with by Buyer, but have not been fulfilled or satisfied by Seller to permit closing by the Closing Date, Seller will be deemed to be in default under this Agreement.

ARTICLE 7

CLOSING

7.1 Time. Provided all conditions set forth in section 6.1 have been either satisfied or waived, the parties shall consummate this transaction no earlier than _ _[*date*]_ _, but on or before _ _[*date*]_ _ (the "Closing"), through the Escrow at the Escrow Holder, on a date selected by Buyer upon 5 days' prior written notice to Buyer, unless the parties shall otherwise agree in writing to an earlier or later date (the "Closing Date"). The Escrow shall be auxiliary to this Agreement, and this Agreement shall neither be merged into nor in any

manner superseded by the Escrow.

7.2 Deposit With Escrow Holder, Escrow Instructions. Buyer and Seller shall promptly open Escrow by delivering to Escrow Holder a fully executed copy of this Agreement, and Buyer shall, together with this Agreement, deliver the Initial Deposit to Escrow Holder, and this Agreement shall serve as the instructions to Escrow Holder for consummation of the purchase and sale contemplated by this Agreement. Seller and Buyer agree to execute such additional and supplementary escrow instructions as may be appropriate to enable Escrow Holder to comply with the terms of this Agreement; provided, however, that in the event of any conflict between the provisions of this Agreement and any supplementary escrow instructions, the terms of this Agreement shall control.

7.3 Closing. The execution and delivery of all documents contemplated under the terms of this Agreement shall be made at the office of the Escrow Holder. The execution and exchange of documents shall take place no later than 2 business days prior to the Closing Date.

7.4 Deliveries to Escrow Holder

(a) By Seller. Seller hereby covenants and agrees to deliver or cause to be delivered to Escrow Holder on or prior to the Closing Date the following instruments and documents, duly executed and, as applicable, acknowledged by Seller:

(i) the Deed;

(ii) the Bill of Sale;

(iii) the Assignment and Assumption of Intangible Property;

(iv) the FIRPTA Affidavit;

(v) a California Franchise Tax Board Form 593-C;

(vi) the Assignment of Leases;

(vii) the Assignment of License Agreement;

(viii) the Assignment of Management Agreement;

(ix) the Legal Opinion or the Seller's Authorization; and

(x) such documents as are necessary under the law to transfer to the Liquor License to Buyer.

(b) By Buyer. Buyer hereby covenants and agrees to deliver or cause to be delivered to Escrow Holder on or before the Closing Date, duly executed by Buyer, if applicable:

(i) the Purchase Price;

(ii) Buyer's closing costs hereunder;

(iii) the amount due after the prorations are computed in accordance with section 7.9;

(iv) the Bill of Sale;

(v) the Assignment and Assumption of Intangible Property;

(vi) the Assignment of Leases;

(vii) the Assignment of License Agreement;

(viii) the Assignment of Management Agreement;

(ix) such documents as are necessary under the law to transfer the Liquor License to Buyer; and

(x) and any and all other documents and instruments to be executed (and, if appropriate, notarized or acknowledged) and delivered by Buyer hereunder.

7.5 Seller's Deliveries Upon Close of Escrow. Seller shall deliver possession of the Property to Buyer upon the Close of Escrow subject only to the Permitted Exceptions. Further, Seller shall deliver to Buyer (or its agents or employees), promptly after the Close of Escrow, originals (or, if originals are not available, copies) of the following items: all Service Contracts, all Leases, the Management Agreement, the License Agreement, all Books, Records, and Plans, all Licenses and Permits, keys to all entrance doors at the Hotel held by Seller (properly tagged for identification), the FIRPTA Affidavit, and any other documents, instruments, data, records, correspondence, or agreements called for under this Agreement, all to the extent not previously delivered, and all to the extent in Seller's actual possession and not available through the Hotel Manager.

7.6 Other Instruments. Seller shall execute and deliver such other instruments, documents, and items as are reasonably required by Escrow Holder, the Title Company, or otherwise, which are required to close the Escrow and consummate the sale of the Property in accordance with the terms of this Agreement.

7.7 Close of Escrow. Provided that Escrow Holder has received the documents and funds described in sections 7.4 and 7.5 hereof, and provided that Escrow Holder has not received prior written notice from either party that any condition set forth herein has not been satisfied or waived, and further provided that the Title Company has issued or is unconditionally prepared and committed to issue to Buyer the Title Policy, Escrow Holder is authorized and instructed:

(a) Recording. At 8:00 a.m. on the Closing Date, to cause the Deed, and any other documents that the parties hereto may mutually direct, to be recorded in the Official Records of the County of _ _[*name*]_ _, State of California, and obtain conformed copies thereof for distribution to Buyer and Seller.

(b) Funds. Once the Deed has been recorded, to disburse all funds deposited with Escrow Holder as follows:

(i) Pay all amounts to be paid by the parties hereunder for Escrow, closing, and title costs and expenses and commissions;

(ii) Disburse the Purchase Price plus other closing credits to Seller; and

(iii) Disburse the excess balance of the funds deposited by Buyer, if any, to Buyer.

(c) Disbursement of Documents to Buyer. Disburse to Buyer any other documents deposited into Escrow by Seller for delivery to Buyer pursuant to this Agreement.

(d) Disbursement of Documents to Seller. Disburse to Seller any other documents deposited into Escrow by Buyer pursuant to this Agreement.

7.8 Notification. If Escrow Holder cannot comply with the instructions herein and to be provided, Escrow Holder is not authorized to cause the recording of the foregoing documents. If Escrow Holder is unable to cause the recording, Escrow Holder shall promptly notify Buyer's attorney, _ _[*name*]_ _, and Seller's attorney, _ _[*name*]_ _.

7.9 Prorations and Adjustments. All Room Revenues and Other Revenues and all operating expenses (*e.g.,* all utilities, *etc.*) that vary based on the actual operations of the Hotel will be prorated as of the Cutoff Time in accordance with the provisions set forth in section 7.11. Advance payments and deposits received by Seller for guest bookings, conventions, meetings, and other Hotel commitments for the period after the Closing Date will be credited to Buyer on the Closing Date. All rents receivable from tenants of the Property earned in or attributable to the period before the Closing Date will be paid to Seller to the extent that such rents have been collected on or before the Closing Date; rents earned in or attributable to the period beginning on the Closing Date and thereafter will be paid to Buyer. Rents receivable from tenants of the Property earned in or attributable to the period before the Closing Date, but received after the Closing will be paid to Seller. Buyer must cooperate with Seller in the collection of these rents. All amounts in the net working capital account for

the hotel operations as of the Closing Date will belong to Seller, and Buyer must replenish such account at Closing or, at Seller's option, credit Seller for such amount at Closing. All operating expenses that are fixed and are typically billed or accrue on a periodic basis and are capable of proration on a per diem basis (*e.g.,* insurance, property taxes, lease rent, *etc*.) will be prorated as of the Cutoff Time in accordance with the provisions set forth in section 7.11. For purposes of calculating prorations, Buyer will be deemed to be in title to the Property (and, thus, entitled to the income and responsible for the expenses) from and after the Cutoff Time. Any apportionments and prorations that are not expressly provided for in this Agreement will be made in accordance with customary practice in _ _[*city*]_ _, _ _[*state*]_ _. Buyer and Seller will prepare a tentative Operations Settlement not later than _ _[*e.g., 3*]_ _ business days before the Closing Date. Under section 7.11, any adjustments to the Purchase Price related to the Personal Property or cash to be funded into Escrow or paid as of the Close of Escrow, subject to adjustment under the final Operations Settlement, must be made by an increase in the amount funded by Buyer into Escrow, and a corresponding increase in the amount to be disbursed to Seller if the prorations result in a net credit to the Seller, or by a decrease in the amount to be funded by Buyer into Escrow, and a corresponding decrease in the amount to be disbursed to Seller if the prorations result in a net credit to the Buyer. A copy of the schedule of adjustments as agreed on by Buyer and Seller will be delivered to Escrow Holder before the Closing Date.

7.10 Closing Statement. Escrow Holder shall prepare a closing statement on or before the Closing Date, as well as all of the cash adjustments as a result of the prorations to be made as of the Close of Escrow generally referred to in section 7.11.

7.11 Operations Settlement. Buyer's and Seller's accountants shall prorate Room Revenues and all Other Revenues as well as all variable operating expenses as of the Cutoff Time, and the results thereof together with a statement of the Tray (Guest) Ledger, the City Ledger, credit card receivables, accounts payable, tax liabilities, cash on hand at the Hotel, Inventory, Expendables, Consumables, and the House Funds shall be set forth in the Operations Settlement, subject to the following:

(a) Taxes. All general real estate and ad valorem personal property taxes and assessments shall be prorated as of the Cutoff Time using the latest available tax rates and assessments. Seller shall be responsible for all general real estate and ad valorem personal property taxes and all special taxes or assessments accruing with respect to the Property for all periods prior to the Cutoff Time, and Buyer shall be responsible for all of such taxes and assessments that accrue after the Cutoff Time. Any tax refunds or rebates that apply to periods before the Cutoff Time shall be the property of Seller.

(b) Utilities. Prior to the Close of Escrow, Seller shall notify all utility companies servicing the Hotel of the anticipated change in ownership of the Hotel and request that all billings after the Close of Escrow be made to Buyer at the Hotel address. Utility meters will be read, to the extent that the utility company will do so, during the daylight hours on the calendar day immediately before the Closing Date, with charges accruing prior to the Cutoff Time paid by Seller and charges accruing thereafter paid by Buyer. Prepaid utility charges shall be prorated on the Closing Statement. Charges for utilities that are metered, or charges for the meters that have not been read by the Closing Date, will be prorated between Buyer and Seller as of the Cutoff Time, if reasonably estimatable or, if not, after the Close of Escrow, based on utility billings received after the Close of Escrow, in which case Seller or Buyer, as appropriate, shall upon receipt submit a copy of the utility billings for any such charges to the other party and such party shall pay its prorata share of such charges to the party requesting payment within _ _[*e.g., 7*]_ _ calendar days from the date of any such request. Seller shall be credited and Buyer debited for all deposits previously made by Seller which the utility company in question will apply to Buyer's account.

(c) Service Contracts. All income and expenses with respect to the Service Contracts that Buyer shall elect to assume upon Closing Date will be prorated as of the Cutoff Time. Seller shall receive a credit for the amount of any prepaid expenses under any Service Contacts.

(d) Reservations. Buyer will honor, for its account, all reservations and Advance Bookings for dates after the Close of Escrow. Buyer authorizes Seller to continue to accept reservations for guest rooms and meeting rooms for periods after the Close of Escrow, provided the terms and conditions of the reservations are in the ordinary course of Seller's business, and Buyer agrees to honor all such reservations in accordance with their terms. Any pre-Closing deposits and Reservation Days made to Seller with respect to confirmed reservations for dates after the Close of Escrow will be credited to Buyer. Any post-Closing deposits received by Seller with respect to confirmed reservations and Reservation Deposits for dates after the Close of Escrow shall be forwarded to Buyer upon receipt by Seller.

(e) House Funds, Tray (Guest) Ledger, and Accounts Receivable. All cash on hand in the Hotel in cash registers, cashiers' "banks", and change funds as of the Cutoff Time shall remain the sole property of Seller and credited (in the amount thereof) to Seller and debited (in the amount thereof) to Buyer. All House Funds shall remain the sole property of Seller and shall be applied and returned to Seller upon the Close of Escrow. All amounts in the Tray (Guest) Ledger (including charges for rooms, telephone charges, and otherwise) accruing prior to the Cutoff Time shall be credited to Seller at face value, and all amounts in the Tray (Guest) Ledger accruing after the Cutoff Time shall belong to Buyer. The entire Tray (Guest) Ledger shall thereupon become the property of Buyer. All amounts in the City Ledger accruing prior to the Cutoff Time shall be credited to Seller at their face amount. All accounts receivable related to customer credit card charges shall be treated in the same manner as the City Ledger, other than Master Charge and Visa accounts, which shall be treated in the same manner as House Funds, and shall remain the property of Seller.

(f) Accounts Payable and Expenses. Subject to the following, all unpaid accounts payable and expenses relating to operations of the Hotel prior to Close of Escrow shall be paid by Seller, or Buyer on behalf of Seller, as the case may be, and there shall be no proration or decrease in the amount to be funded into Escrow pursuant to section 7.4(b) as a result such payments. By way of illustration, Seller shall pay (i) accounts payable and expenses relating to Personal Property, Inventory, or otherwise; (ii) expenses arising from items not a part of Inventory (*e.g.,* energy, utilities, insurance, advertising, trade association dues, subscriptions, *etc.*); and (iii) services provided (*e.g.,* by independent contractors, professionals, other consultants, and vendors pursuant to Service Contracts, *etc.*). Buyer alone shall be responsible for all accounts payable related to Personal Property, inventory, or otherwise to the extent not yet rendered, as of the Close of Escrow, providing same are incurred in the ordinary course of business, and such Personal Property, inventory or other items are delivered, and/or such services rendered, after the Close of Escrow. In addition to the foregoing, all accounts payable and expenses relating to operations of the Property after the Close of Escrow will be paid by Buyer. Prepaid expenses with respect to all such items as of the Close of Escrow shall be credited to Seller.

(g) Employees. All employment compensation accrued as of the Cutoff Time shall be paid by Seller. Under section 5.6, upon the Close of Escrow all of Seller's employees at the Hotel (if any) shall be terminated by Seller, and at the option of Buyer rehired by Buyer on such terms and in such capacity as may be agreed by Buyer and each such employee, it being understood that Buyer is not assuming any accrued liabilities or obligations with respect to such employees. Any termination of such employees shall be undertaken by Seller prior to the Close of Escrow at the sole cost, expense, and liability of Seller. Employees of _ _[*name of manager*]_ _ shall remain employees of _ _[*name of manager*]_ _.

(h) Other Costs and Expenses. Seller shall pay one-half of the cost for a standard owner's policy (with no endorsements). Buyer shall pay all other premiums for the Title Policy and any endorsements thereto required by Buyer that the Title Company is willing to issue. Seller shall pay all sales taxes applicable to the sale of the Personal Property. Seller shall pay any documentary or other transfer taxes applicable to the sale, if any. Seller and Buyer shall share equally all other costs and charges of Escrow and any attorneys' fees and inspection fee charged by _ _[*name of licensor/franchisor*]_ _, and/or _ _[*name of manager*]_ _.

7.12 Consumables. As of the Cutoff Time on the Closing Date, Buyer and Seller shall take an inventory of all the Consumables. All food and beverages purchased by Seller in the ordinary course of business prior to such time but delivered to the Hotel thereafter shall be deemed to have been purchased by Seller for the account of Buyer, who shall make payment therefor.

7.13 Licenses/Governmental Certificates and Approvals. Buyer shall be fully responsible for and shall pay all costs and fees required to be paid in connection with transfer of any and all Licenses and Permits currently held by Seller, and shall pay all governmental transfer and license fees in connection with such transfers, as well as applying for and obtaining any and all new licenses, permits, certificates, and/or approvals necessary or appropriate in connection with the operation of the Hotel and the consummation of the purchase and sale of the Property, subject only to section 7.11(h). Buyer shall prosecute its applications in accordance with the rules and procedures set forth under applicable law. Seller shall cooperate as may be reasonably necessary to assist Buyer in obtaining the transfer or issuance of such licenses, permits, certificates, and approvals. Buyer shall use reasonable efforts to cause Seller to be released from any liability relating to any Licenses and Permits to be transferred as of the Close of Escrow.

7.14 Adjustments. If any of the payments at closing are based on estimated prorations, the parties agree to make final adjustments to such prorated amounts within _ _[*e.g., 30*]_ _ days after Closing.

7.15 Safe Deposit Boxes and Baggage Check

(a) Any baggage or other property of departed guests held by Seller will remain at the Hotel in the custody of the general manager of the Hotel ("General Manager") for a period not to exceed _ _[*e.g., 90*]_ _ days after the Cutoff Time. After such period, all such baggage or property will, at the option of Seller, be removed by Seller or abandoned by Seller, and Buyer may dispose of such baggage in any manner deemed appropriate by Buyer in its sole and absolute discretion. Seller agrees to indemnify, defend, and hold Buyer harmless against all claims, losses, and liabilities that Buyer may suffer, sustain, or incur in connection with baggage or other property left at the Hotel by departed guests before the Cutoff Time, except that Buyer will be responsible for holding for said period such baggage and other property of departed guests as has been placed into the General Manager's custody as of the Cutoff Time. All baggage of guests who are still in the Hotel as of the Cutoff Time that has been checked with or left in the care of Seller will be inventoried jointly by Seller and Buyer. Buyer agrees to indemnify, defend, and hold Seller harmless against all claims, losses, or liabilities that Seller may suffer, sustain, or incur with respect to such inventoried baggage arising out of acts or omissions of Buyer after the Cutoff Time. Seller agrees to indemnify, defend, and hold Buyer harmless against all claims, losses, or liabilities that Buyer may suffer, sustain, or incur with respect to such inventoried baggage arising out of the acts or omissions of Seller before the Cutoff Time and all claims with respect to baggage or other property allegedly left at the Hotel before the Cutoff Time but not so tagged and inventoried.

(b) Not later than _ _[*e.g., 5*]_ _ days before the Cutoff Time, Seller will send, or cause the General Manager to send, written notice to guests or other persons who have safe deposit boxes at the Hotel, advising of the sale of the Hotel and requesting verification or removal of the contents within _ _[*e.g., 5*]_ _ days. The safe deposit boxes of guests or other persons who have not responded to said written notice as of the Cutoff Time will be opened only in the presence of the General Manager and representatives of both Seller and Buyer. The contents of all boxes opened as aforesaid will be listed at the time such boxes are opened and each such list must be signed by or on behalf of the General Manager, and Buyer will not be liable or responsible for any items claimed to have been in said boxes unless such items are included in such list. Seller agree to indemnify, defend, and hold Buyer harmless from and against any claims, losses, or liabilities that Buyer may suffer, sustain, or incur with respect to any items claimed to have been in safety deposit boxes but not included on such list. Buyer agrees to indemnify, defend, and hold Seller harmless from and against any claims, losses, or liabilities that Seller may suffer, sustain, or incur with respect to items claimed to have been in safety deposit boxes and included in such list.

7.16 Indemnification

(a) Seller agrees to defend, indemnify, and hold Buyer harmless from and against any and all loss, damage, cost, claim liability, or expense (including court costs and reasonable attorney fees) suffered or incurred by Buyer as a result of Seller's failure to pay any accounts payable or any sales, use, or occupancy taxes due in connection with the rental of rooms, the sale of goods, or the performance of services before the Cutoff Time, or arising out of any event occurring on or before the Cutoff Time, or any liability or obligation respecting the Property existing as of the Cutoff Time and not assumed by Buyer under this Agreement, except to the extent Buyer has received a credit therefor against the Purchase Price under this Agreement.

(b) Buyer agrees to defend, indemnify, and hold Seller harmless from and against any and all loss, damage, cost, claim, liability, or expense (including court costs and reasonable attorney fees) suffered or incurred by Seller arising out of any events relating to the period following the Cutoff Time or any liability or obligation assumed by Buyer under this Agreement or in any agreement executed and/or delivered at the Closing, or resulting from Buyer's failure to pay any item for which it received a credit against the Purchase Price under this Agreement.

ARTICLE 8

TERMINATION

8.1 Termination. If at the Closing (i) Seller is unable to sell the Property in accordance with all of the terms, provisions, and conditions of this Agreement, or (ii) any of the conditions to Buyer's obligations under this Agreement shall not be satisfied, then Buyer shall have the right:

(a) To cancel this Agreement by giving notice to Seller, and this Agreement shall be deemed to be

terminated as of the date of such notice, and Buyer shall be entitled to an immediate return of the Deposit together with all interest earned on it, if any; or

(b) To take title to the Property subject to any defect, exception, objection, inaccuracy, or failure and receive a credit against the Purchase Price in an amount equal to the cost of removing the defect, exception, objection, or inaccuracy and the cost of curing any such failure.

8.2 Remedies of Buyer. None of the foregoing provisions of this Article 8 shall limit or affect any other rights or remedies available to Buyer at law or in equity in the event of a default by Seller under this Agreement. In addition to all other rights or remedies available to Buyer at law or in equity, Buyer is hereunder given the right of specific performance in the event of a default by Seller in the performance of its obligations under this Agreement.

8.3 Default of Buyer. SHOULD BUYER DEFAULT IN ITS OBLIGATIONS TO PURCHASE THE PROPERTY UNDER THE TERMS OF THIS AGREEMENT, BUYER AND SELLER AGREE THAT IT WOULD BE IMPRACTICAL OR EXTREMELY DIFFICULT TO FIX ACTUAL DAMAGES AND THAT THE DEPOSIT CONSTITUTES A REASONABLE ESTIMATE, UNDER THE CIRCUMSTANCES EXISTING AT THE TIME THIS AGREEMENT IS MADE, OF THE DAMAGES SELLER WOULD SUSTAIN BECAUSE OF SUCH DEFAULT. IN THE EVENT OF ANY SUCH DEFAULT, SELLER SHALL RETAIN THE DEPOSIT, AND ANY INTEREST ACCRUED THEREON AS LIQUIDATED DAMAGES. RETENTION OF THE DEPOSIT AND ANY INTEREST ACCRUED THEREON SHALL BE SELLER'S SOLE AND EXCLUSIVE REMEDY IN THE EVENT OF BUYER'S DEFAULT, AND IN SUCH EVENT BUYER SHALL HAVE NO FURTHER LIABILITY TO SELLER UNDER THIS AGREEMENT.

WE ACKNOWLEDGE THIS LIQUIDATED DAMAGES CLAUSE:

SELLER'S INITIALS _____

BUYER'S INITIALS _____

ARTICLE 9

DAMAGE, DESTRUCTION, AND CONDEMNATION

9.1 Damage or Destruction

(a) Except as specifically provided in this Article 9, destruction, damage, or condemnation of all or any part of the Property prior to the Closing Date shall be governed by the terms of the Uniform Vendor and Purchaser Risk Act, _ _[*cite state statute*]_ _ *et seq.* In the event of any damage to the Property prior to the Close of Escrow, Seller shall promptly notify Buyer of such damage. If the estimated cost of repair or restoration is _ _[*dollar amount*]_ _ or less, Buyer shall accept conveyance of the Property in such damaged condition, and Seller shall pay to Buyer at the Closing all insurance proceeds previously received by Seller in respect of such casualty and assign and transfer to Buyer, at the Closing, all right, title, and interest of Seller in and to the policies of insurance covering such damage or casualty, and in and to the proceeds of those policies that Seller may be entitled to receive. If the proceeds under said insurance policies are net of any deductible or do not otherwise adequately cover the cost of full restoration or repair of the damaged Property, then Buyer shall have the option to either (i) cancel this Agreement, in which event it shall have the rights set forth in section 8.1(a), or (ii) accept the Property "as is" together with said insurance proceeds.

(b) Notwithstanding anything to the contrary contained in this section 9.1, if the estimated cost of repair or restoration of any damaged Property shall exceed _ _[*dollar amount*]_ _, Buyer may at its option, to be exercised at any time after receipt of notice of such casualty, either (i) cancel this Agreement, in which event it shall have the rights set forth in section 8.1(a), or (ii) accept the Property "as is", in which event Seller shall pay to Buyer at Closing all insurance proceeds previously received by Seller in respect of such casualty and assign and transfer to Buyer at Closing all right, title, and interest of Seller in and to the policies of insurance covering such damage or casualty, and in and to the proceeds of those policies that Seller may be entitled to receive.

9.2 Condemnation

(a) In the event of the institution of any proceedings, judicial, administrative, or otherwise, that shall

relate to the proposed taking of any material portion of the Hotel Property by eminent domain or in condemnation, whether of fee title or otherwise, and whether permanent or temporary, or if any such proceeding be threatened or contemplated or in the event of the taking of any material portion of the Property by eminent domain prior to the Closing, Buyer shall have the right and option to terminate this Agreement by giving Seller written notice to such effect any time after receipt of written notice of any such occurrence(s). Seller hereby agrees to furnish Buyer with written notification in respect of any such proceeding within 48 hours from Seller's receipt of any such notification, unless receipt of such notification is received within 48 hours of the Closing, in which case Buyer shall be furnished with such written notification prior to the Closing. Seller agrees to keep Buyer informed of the progress of any proceedings referred to or contemplated by this section 9.2 and any negotiations relating to any threatened or contemplated condemnation, and agrees not to make any settlement or arrangement with respect thereto without the prior written consent of Buyer. Should Buyer so terminate this Agreement, Buyer shall have the rights set forth in section 8.1(b). For the purposes of this section 9.2, a "material portion" means any portion of the Property the taking of which would materially and adversely affect the ownership and operation of the Property as contemplated by Buyer.

(b) If Buyer does not elect to terminate as permitted by subparagraph (a) above, or if a nonmaterial portion of the Property is taken, then this Agreement shall remain in full force and effect and Seller will turn over or credit to Buyer at the closing all monies received by Seller by reason of such taking and shall further assign to Buyer all of Seller's right, title, and interest in and to any awards that may be made for such taking.

ARTICLE 10

GENERAL

10.1 Notices. Any notices relating to this Agreement shall be given in writing and shall be deemed sufficiently given and served for all purposes when delivered personally or by generally recognized overnight courier service, or 5 days after deposit in the United States mail, certified or registered, return receipt requested, with postage prepaid, addressed as follows:

SELLER:_____

with a

copy to:_____

BUYER:_____

with a

copy to:_____

Either party may change its address by written notice to the other given in the manner set forth above.

10.2 Entire Agreement. The terms of this Agreement are intended by the parties as a final expression of their agreement with respect to such terms as are included in this Agreement and may not be contradicted by evidence of any prior or contemporaneous agreement. This Agreement specifically supersedes any prior written or oral agreements between the parties. The language in all parts of this Agreement shall be construed as a whole in accordance with its fair meaning.

10.3 Amendments and Waivers. No addition to or modification of this Agreement shall be effective unless set forth in writing and signed by the party against whom the addition or modification is sought to be enforced. The party benefited by any condition or obligation may waive the same, but such waiver shall not be enforceable by another party unless made in writing and signed by the waiving party.

10.4 Invalidity of Provision. If any provision of this Agreement as applied to either party or to any circumstance shall be adjudged by a court of competent jurisdiction to be void or unenforceable for any reason, that shall in no way affect (to the maximum extent permissible by law) any other provision of this Agreement, the application of any such provision under circumstances different from those adjudicated by the court, or the validity or enforceability of this Agreement as a whole.

10.5 No Merger. This Agreement, and each of the provisions hereof and all warranties and representations contained herein, shall survive the Closing and shall not merge in any instrument conveying title to Buyer. All representations, warranties, agreements, and obligations of the parties shall, notwithstanding any investigation made by any party to this Agreement, survive Closing, and the same shall inure to the benefit of and be binding upon the respective successors and assigns of the parties.

10.6 References. Unless otherwise indicated, (a) all Article and section references are to the articles and sections of this Agreement, and (b) all references to days are to calendar days. Whenever under the terms of this Agreement the time for performance of a covenant or condition falls on a Saturday, Sunday, or California state holiday, such time for performance shall be extended to the next business day. The headings used in this Agreement are provided for convenience only and this Agreement shall be interpreted without reference to any headings. The date of this Agreement is for reference purposes only and is not necessarily the date on which it was entered into.

10.7 Governing Law. This Agreement shall be governed by the laws of the State of California applicable to contracts made and to be performed in California.

10.8 Confidentiality and Publicity. Before the Closing, the parties shall at all times keep this transaction and any documents received from each other confidential, except to the extent necessary to (a) comply with applicable law and regulations, or (b) carry out the obligations set forth in this Agreement. Any such disclosure to third parties shall indicate that the information is confidential and should be so treated by the third party. Prior to the Closing, no press release or other public disclosure may be made by Buyer or any of its agents concerning this transaction without the prior written consent of Seller.

10.9 Time. Time is of the essence in the performance of the parties' respective obligations under this Agreement.

10.10 Right of Access. At any time prior to the Closing Date, Buyer and its authorized representatives, agents, employees, accountants, contractors, appraisers, architects, and engineers shall have the right to (a) inspect the Property, (b) examine and copy Seller's books and records relating to the Property, and (c) have access to tenants of the Property.

10.11 Attorney Fees. In the event of any legal or equitable proceeding for enforcement of any of the terms or conditions of this Agreement, or any alleged disputes, breaches, defaults, or misrepresentations in connection with any provision of this Agreement, the prevailing party in such action, or the nondismissing party where the dismissal occurs other than by reason of a settlement, shall be entitled to recover its reasonable costs and expenses, including without limitation reasonable attorney fees and costs of defense paid or incurred in good faith. The "prevailing party," for purposes of this Agreement, shall be deemed to be that party who obtains substantially the result sought, whether by settlement, dismissal, or judgment.

10.12 Assignment. This Agreement shall inure to the benefit of and be binding upon the parties hereto and their respective successors and assigns. However, Buyer shall have the right to assign all or any portion of its interest in this Agreement without Seller's prior written consent, provided that Buyer shall remain liable hereunder for the performance of Buyer's obligations hereunder. Any assignment of this Agreement in whole or in part in which Buyer is to be released of its obligations hereunder shall require the consent of Seller, in its sole and absolute discretion, and shall not delay the Closing.

10.13 No Third Party Beneficiaries. Nothing in this Agreement, express or implied, is intended to confer any rights or remedies under or by reason of this Agreement on any person other than the parties to it and their respective permitted successors and assigns, nor is anything in this Agreement intended to relieve or discharge any obligation of any third person to any party hereto or give any third person any right of subrogation or action over against any party to this Agreement.

10.14 Remedies Cumulative. The remedies set forth in this Agreement are cumulative and not exclusive to any other legal or equitable remedy available to a party.

10.15 Commissions; Indemnity. Pursuant to a separate agreement, Buyer shall pay _ _[*name(s) of broker(s)*]_ _ for _ _[*its/their*]_ _ services as brokers in this transaction. Except as provided in this section 10.15, neither party has had any contact or dealings regarding the Property, or any communication in connection with the subject matter of this transaction, through any other licensed real estate broker or other person who can

claim a commission or finder's fee as a procuring cause of the sale contemplated herein. In the event that any other broker or finder perfects a claim for a commission or finder's fee based on any contract, dealings, or communication with Buyer or Seller, then such party shall indemnify, defend, and hold the other party harmless from all costs and expenses (including reasonable attorney fees and costs of defense) incurred in connection with such claim.

10.16 Counterparts. This Agreement may be executed in one or more counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

ARTICLE 11

DEFINITIONS

11.1 Definitions. For purposes of this Agreement, the parties agree that the following terms shall have the following meanings:

(a) "Advance Booking Agreements" means contracts or agreements for Advance Bookings.

(b) "Advance Bookings" means all agreements, bookings, or other confirmed reservations for public functions, banquets, or the use of rooms in the Hotel or other Hotel facilities or services for the period after the "Closing Date" as identified on the Advance Bookings Schedule (as that term is defined in section 3.1(t)) and all similar arrangements hereafter entered into by Seller in connection with the Hotel as permitted by section 4.1 of this Agreement.

(c) "Agreement" means this Hotel Purchase and Sale Agreement between Seller and Buyer, providing for the purchase and sale of the Property.

(d) "Assignment and Assumption of Intangible Property" means that certain Assignment and Assumption of Intangible Property, to be executed by Seller and Buyer, assigning to Buyer all of Seller's right, title, and interest in and to the Intangible Property, substantially in the form of Exhibit E attached hereto.

(e) "Assignment of Leases" means an Assignment and Assumption of Leases in the form or substantially the form of the attached Exhibit F.

(f) "Assignment of License Agreement" means an Assignment and Assumption of the License Agreement in the form of the attached Exhibit G, with such changes as may reasonably be requested by _ _[*name of manager*]_ _ **or** _ _[*name of licensor/franchisor*]_ _**, as the case may be.**

(g) "Assignment of Management Agreement" means an Assignment and Assumption of the Management Agreement in the form of, or substantially the form of, the attached Exhibit H, with such changes as may reasonably be requested by _ _[*name of manager*]_ _ **or** _ _[*name of licensor/franchisor*]_ _**, as the case may be.**

(h) "Bill of Sale" means a Bill of Sale to be executed by Seller, conveying to Buyer all of Seller's right, title, and interest in and to all Personal Property.

(i) "Books, Records, and Plans" means (i) the books, records, guest and customer lists for the Hotel, files, reports, surveys, studies, projections, budgets, and strategic plans of Seller in connection with the ownership operation, maintenance, and management of the Property and the Hotel, (ii) plans and specifications respecting the Property, and (iii) structural reviews, architectural drawings, and engineering, soil, seismic, geologic, and architectural reports, studies, certificates, and other documents pertaining to the Improvements, including without limitation any Phase I environmental reports.

(j) "City Ledger" means all accounts receivable of guests and patrons of the Hotel who have received hotel services but not yet paid their bills (other than the Tray (Guest) Ledger) which have been outstanding as of the Close of Escrow for not more than 90 days.

(k) "Claims" means claims, actions, causes of action, demands, liabilities, liens, costs, expenses, penalties, damages, and losses, including, without limitation, attorney fees and costs, against Seller in connection with the ownership or operation of the Property or the Hotel, including those Claims listed on the

Claims Schedule (as that term is defined in section 3.1(m)).

(l) "Close of Escrow" means the completion of the actions described in section 7.7.

(m) "Closing" is defined in section 7.1.

(n) "Closing Date" means the date as set forth in section 7.1.

(o) "COBRA" is defined in section 5.5(b).

(p) "Code" means the United States Internal Revenue Code of 1986, as amended.

(q) "Consumables" means all reserve stocks of food and beverages at the Hotel.

(r) "Contract Rooms Schedule" is defined in section 3.1(u).

(s) "Cutoff Time" means 3:00 a.m. on the Closing Date.

(t) "Deed" means that certain limited warranty deed, to be executed and acknowledged in recordable form by Seller, conveying Seller's interest in the Real Property to Buyer.

(u) "Due Diligence Approval" is defined in section 2.2.

(v) "Employee Schedule" is defined in Section 5.2.

(w) "Equipment Leases" means all leases or other rental agreements for the use of any of the Furniture and Equipment and Expendables, all as identified on the Equipment Lease Schedule (as that term is defined in section 3.1(n)) and those leases of Furniture and Equipment and Expendables hereafter made in connection with the Hotel as permitted by the provisions of section 4.1 of this Agreement.

(x) "Escrow" is defined in section 1.3.

(y) "Escrow Holder" is defined in section 1.3.

(z) "Expendables" means all blankets, linens, tableware, china, glassware, silverware, uniforms, and other goods of an expendable nature owned or leased by Seller in connection with the ownership, operation, or maintenance of the Hotel and located or customarily located at the Hotel, including those items identified on Schedule 14 (the "Expendables Schedule") attached hereto and such replacements as are permitted or required by this Agreement, all in such quantities as may be prescribed herein.

(aa) "FIRPTA Affidavit" means that certain non-foreign affidavit executed and sworn under penalty of perjury by Seller, substantially in the form of Exhibit I attached hereto.

(bb) "Fixtures" means all fixtures affixed or attached to the Real Property or Improvements but shall not include fixtures owned by tenants or other occupants of the Real Property.

(cc) "Furniture and Equipment" means all personal property, including telephones, typewriters, mattresses, computers, software, televisions, appliances, tools, art work, furniture, furnishings, machinery, vehicles, and other personal property and equipment owned or leased by Seller in connection with the ownership, operation, or maintenance of the Hotel located or customarily located at the Hotel (but excluding fixtures), including those items identified on the Furniture and Equipment Schedule (as that term is defined in section 3.1(v)) and such replacements as are permitted or required by this Agreement, all in such quantities as may be prescribed herein; provided, however, that Furniture and Equipment shall not include Inventory, Consumables, or Expendables.

(dd) "General Manager" is defined in section 7.15.

(ee) "Goodwill" means all goodwill related to the Property or the operation of the Hotel including, without limitation, all right, title, and interest in the telephone number and listings of the Hotel, all video tapes,

films, brochures, and other advertising and promotional materials of any kind or nature used in connection with the advertising of the Hotel.

(ff) "Hazardous Materials" is defined in section 3.1(k).

(gg) "Hotel" means that certain _ _[*e.g., 300*]_ _-key hotel building and all accessory buildings and structures owned by Seller and located on the Land, commonly known as the "_ _[*name of hotel*]_ _" and located at _ _[*address*]_ _.

(hh) "House Funds" means cash on hand in the Hotel's operating accounts and in reserve accounts for Furniture and Equipment, and restricted and other cash accounts (*e.g.,* payroll accounts, replacement or reserve accounts, credit card accounts, money market accounts, petty cash bank accounts, travel agent commission accounts, and accounts for excess operating funds) maintained by Seller or the hotel operator with respect to the Hotel as of the Cutoff Time.

(ii) "Improvements" means Seller's interest in any buildings, systems, facilities, structures, fences, parking areas, machinery, equipment, apparatus, and appliances attached to and used in connection with the operation or occupancy of the Land, such as heating and air-conditioning systems, refrigeration, ventilation, garbage disposal, utility conduits, or other improvements located upon the Land, including without limitation the Hotel.

(jj) "Insurance Policies Schedule" is defined in section 3.1(l).

(kk) "Intangible Property" means the Service Contracts, the Equipment Leases, the Reservation Deposits, the Goodwill, the Books and Records, the Advance Bookings, and the Intellectual Property.

(ll) "Intellectual Property" means all copyrights, logos, designs, trademarks, trade names, service marks, and other intellectual property used in connection with the ownership and operation of the Hotel and owned by Seller, including without limitation all rights to telephone numbers for the Hotel.

(mm) "Inventory" means all stock in trade of the Hotel and operating inventories (including stationery, office supplies, soap and other guest supplies, fuel for furnaces and cleaners, cleaning compounds and preparations, and other operational and maintenance supplies) located or customarily located at the Hotel (and which shall total at least 2 weeks of guestroom and office supplies and two and one-half times the daily usage of linens) and till money (which shall be calculated and treated as an adjustment item pursuant to section 7.11 hereof); provided, however, that Inventory shall not include Expendables or Consumables.

(nn) "Land" means the real property consisting of approximately _ _[*number of square feet*]_ _ square feet as more particularly described in Exhibit A attached hereto, together with Seller's interest, if any, in (a) all privileges, rights, easements, and appurtenances belonging to the real property, including without limitation all minerals, oil, gas, and other hydrocarbon substances on and under the real property, (b) all development rights, air rights, water, water rights, and water stock relating to the real property and (c) all rights, title, and interest of Seller in and to any streets, alleys, passages, other easements, and other rights-of-way or appurtenances included in, adjacent to, or used in connection with the real property.

(oo) "Leases" means Seller's interest, as landlord, under all leases of space in the Improvements, including without limitation all occupancy agreements, concession agreements, and restaurant operating or lease agreements, including those Leases listed on the Lease Schedule (as that term is defined in section 3.1(w)).

(pp) "Legal Opinion" is defined in section 6.1(q).

(qq) "License Agreement" means that License and Franchise Agreement dated _ _[*date*]_ _ between _ _[*name*]_ _ as licensor and franchisor and Seller as Owner.

(rr) "License Agreement Estoppel Certificate" is defined in section 6.1(d).

(ss) "Licenses and Permits" means all building and other permits, certificates, licenses, franchises, authorizations, and approvals granted by any governmental authority obtained or held by Seller that are necessary in connection with the ownership, construction, occupancy, operation, or use of the Property and

the Hotel in full compliance with all applicable laws, ordinances, and statutes, a list of which is set forth on the Licenses and Permits Schedule (as that term is defined in section 3.1(p)).

(tt) "Liquor License" means the _ _[*describe type of license, e.g., Type 47 on-sale general or eating place liquor license*]_ _ liquor license issued to Seller by the California Department of Alcoholic Beverage Control.

(uu) "Litigation Schedule" is defined in section 6.1(m).

(vv) "Management Agreement" means that Management Agreement dated _ _[*date*]_ _ between _ _[*name*]_ _, as Manager and Seller as Owner.

(ww) "Management Agreement Estoppel Certificate" is defined in section 6.1(e).

(xx) "Operations Settlement" means a final accounting of the prorations under section 7.11, prepared by Seller's and Buyer's accountants during the period beginning at _ _[*e.g., 8:00 p.m.*]_ _ of the evening immediately before the Cutoff Time and _ _[*e.g., 8:00 a.m.*]_ _ of the morning immediately following the Cutoff Time, the results of which shall be incorporated into the Operations Settlement, which shall be executed by Buyer and Seller.

(yy) "Other Property" means all other assets, properties, rights, and claims of Seller that are used or held for use in connection with the Hotel of every kind and description, wherever located, tangible or intangible, vested or unvested, contingent or otherwise, as the same shall exist on the Closing Date, whether or not specifically enumerated or identified herein or in any of the exhibits or schedules annexed hereto or delivered hereunder or in any other documents provided to Buyer hereunder.

(zz) "Other Revenues" means all revenues earned from the operation of the Hotel, other than Room Revenues, including, without limitation, rental of meeting and banquet rooms, telephone sales, pay television sales, valet and parking services, and other similar revenues, together with any sales tax or other taxes thereon.

(aaa) "Partner Approval Date" is defined in section 6.2(d).

(bbb) "Permits and Licenses" means all permits, licenses, and other government authorizations required or necessary for the lawful operation of the Hotel.

(ccc) "Permitted Exceptions" is defined in section 6.1(c), together with the Title Company's standard printed title policy exceptions and exclusions.

(ddd) "Personal Property" means the Tangible Property and the Intangible Property.

(eee) "Preliminary Report" is defined in section 2.1(a).

(fff) "Property" shall include the items referred to in section 1.1.

(ggg) "Purchase Price" is defined in section 1.2.

(hhh) "Real Property" means the Land, the Improvements (including without limitation the Hotel), and the Fixtures.

(iii) "Rent Roll" is defined in section 2.1(k).

(jjj) "Reservation Deposits" means all deposits taken from guests, groups, conventions, or others, and any other amounts prepaid in connection with services to be rendered on or after the Closing Date as identified on the Reservation Deposit Schedule (as that term is defined in section 3.1(t)) and all deposits and similar amounts hereafter taken by Seller in connection with the Hotel as permitted by section 4.1 of this Agreement.

(kkk) "Room Revenues" means all revenues from the rental of guest rooms of the Hotel (but excluding any items included in the definition of Other Revenues), together with any sales or other taxes thereon.

(lll) "Seller's knowledge" or "knowledge of Seller" means the actual knowledge of _ _[*name*]_ _ and _ _[*name*]_ _ without investigation or inquiry.

(mmm) "Service Contracts" means all service contracts, maintenance agreements, supply, and other contracts for the provision of services, materials, or supplies to or for the benefit of the Hotel delivered to Buyer under the provisions of section 2.1(c), including without limitation those listed on the Service Contract Schedule (as that term is defined in section 3.1(o)) and including any guaranties of performance and warranties, and those other similar agreements hereafter made in connection with the Hotel as permitted by the provisions of section 4.1 of this Agreement; provided, however, that Service Contracts shall not include Equipment Leases.

(nnn) "Survey" is defined in section 2.1(b).

(ooo) "Tangible Property" means the Furniture and Equipment, the Liquor License, the Inventory, the Expendables, and the Consumables.

(ppp) "Title Company" is defined in section 2.1(a).

(qqq) "Title Policy" is defined in section 6.1(c).

(rrr) "Tray (Guest) Ledger" means any accounts of guests of the Hotel who have not checked out as of the Cutoff Time.

(sss) "Union Contracts" means union collective bargaining contracts, labor agreements, and collective bargaining agreements, together with all supplements, amendments and modifications thereto.

11.2 References. All references in this Agreement to particular sections or articles shall, unless otherwise expressly provided or unless the context otherwise requires, be deemed to refer to the specific sections or articles in this Agreement. In addition, the words "hereof," "herein," "hereunder," and words of similar import refer to this Agreement as a whole, and not to any particular section or article. The words "include" or "including" shall be construed as incorporating, also, "but not limited to" or "without limitation".

IN WITNESS WHEREOF, the parties have executed this Agreement as of the Effective Date.

BUYER: _ _[*Name of entity*]_ _,
a _ _[*specify type of entity*]_ _

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its President

SELLER: _ _[*Name of entity*]_ _,
a _ _[*specify type of entity*]_ _

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Its President

TABLE OF EXHIBITS

EXHIBIT	TITLE
A	Legal Description
B	License Agreement Estoppel Certificate
C	Management Agreement Estoppel Certificate
D	Tenant Estoppel Certificates

E **Assignment and Assumption of Intangible Property**

F **Assignment of Leases**

G **Assignment of License Agreement**

H **Assignment of Management Agreement**

I **FIRPTA Affidavit**

TABLE OF SCHEDULES

Schedule 1 **Insurance Policies Schedule**

Schedule 2 **Claims Schedule**

Schedule 3 **Equipment Lease Schedule**

Schedule 4 **Service Contract Schedule**

Schedule 5 **Licenses and Permits Schedule**

Schedule 6 **Advance Bookings Schedule**

Schedule 7 **Reservation Deposit Schedule**

Schedule 8 **Contract Rooms Schedule**

Schedule 9 **Furniture and Equipment Schedule**

Schedule 10 **Lease Schedule**

Schedule 11 **Employee Schedule**

Schedule 12 **Litigation Schedule**

Schedule 13 **Employee Plans Schedule**

Schedule 14 **Expendables Schedule**

© The Regents of the University of California

Appendix R

Estoppel Certificate From Hotel Operator

▶ To download **Word** version, right click and choose *Save Target As*

▶ To download **WordPerfect** version, right click and choose *Save Target As*

Note: This form is being provided as a sample. It has not been reviewed or edited by CEB. The reader should carefully review and conform it to the circumstances of his or her transaction. CEB is grateful to Timothy N. Brown and Anthony Theophilos for providing this form.

To: _ _[*name*]_ _ (Lender)

And _ _[*name*]_ _, a _ _[*type of entity*]_ _ and its assigns (Buyer)

Re: Hotel Management Agreement for _ _[*name*]_ _ Hotel (Agreement) between _ _[*name*]_ _, a _ _[*type of entity*]_ _, as Owner (Owner) and _ _[*name*]_ _, a _ _[*type of entity*]_ _ (Operator), dated as of _ _[*date*]_ _, for the management of a hotel and related facilities in _ _[*city*]_ _, California known as "_ _[*name of hotel*]_ _" and the other facilities as described in the Agreement (Hotel), as amended by the following amendments: _ _[*list all amendments; if none, insert "None"*]_ _.

Ladies and Gentlemen:

Operator hereby certifies to Buyer and Lender as follows (capitalized terms not defined in this estoppel are defined in the Agreement):

1. The Agreement is in full force and effect; there are no amendments or modifications of any kind to the Agreement; other than _ _[*list all amendments; if none, insert "None"*]_ _, there are no other promises, agreements, understandings, or commitments between Owner and Operator relating to the Hotel or the Real Property; and Operator has not given Owner any notice of termination under the Agreement, as amended;

2. There has not been and is now no assignment by Operator of the Agreement, or any rights in the Agreement, to any party;

3. As of the date of this Estoppel, Operator has no charge, lien, or claim of offset under the Agreement and Owner does not owe any sums to Operator under the Agreement, including without limitation Base Fees for periods prior to the first day of the month in which this Estoppel was executed or Incentive Fees for any calendar year prior to _ _[*year*]_ _ (Incentive Fees for _ _[*year*]_ _ remain payable in accordance with the terms of the Agreement) or under any other agreement, document, or judgment except as set forth below:

4. As of the date of this Estoppel, Operator has not delivered any written notice of any uncured default, event of default, or breach by Owner under the Agreement, and Operator has no actual knowledge of any facts or circumstances that, with the passage of time, will constitute a default, event of default, or breach under the Agreement, except as set forth below. Operator has made no claim against Owner alleging Owner's default under the Agreement.

[*List defaults or breaches; if none, insert "None"*];

5. To the best of Operator's knowledge, Operator has received no written notice that the Hotel fails to comply with all current requirements of applicable building and zoning laws and regulations;

6. Owner does not owe any sums to Operator pursuant to Section _ _ of the Agreement, which requires Owner to reimburse Operator for Reimbursable Expenses, except as set forth below: _ _[*List sums owed; if none, insert "None"*]_ _;

7. As of the date of this Estoppel, there are sufficient Furniture and Equipment, Inventory, Expendables, and Consumables (including items that may have been ordered but not yet received or not yet paid for) owned by the Owner and under the control of the Operator necessary to operate the Hotel in accordance with the Agreement;

8. As of the date of this Estoppel, the amount of the Reserve Account is _ _[*dollar amount*]_ _, the amount of the Reserve Fund is _ _[*dollar amount*]_ _ and the amount of the Working Capital Balance is _ _[*dollar amount*]_ _;

9. During the period beginning January 1, _ _[*year*]_ _, and ending the date of this Estoppel, the amount of funds deposited into the Reserve Account was _ _[*dollar amount*]_ _, representing _ _[*number*]_ _ percent of Gross Revenues for such period;

10. The Capital Expenditure Budget under the Agreement for _ _[____]_ _ is _ _[*dollar amount*]_ _ and the amount of such Capital Expenditure Budget for _ _[____]_ _ that has been disbursed as of the first day of the month in which this certificate was executed is _ _[*dollar amount*]_ _;

11. Operator employs all of the staff and other personnel operating the Hotel (Employees); there are no collective bargaining agreements in force or being negotiated with respect to the Employees; all sums due and owing prior to the date of this Estoppel for all employee benefit plans for the Employees have been paid or will be paid in the ordinary course when due by Operator and all wages, salaries, and other sums payable to the Employees have been paid or will be paid in the ordinary course when due by Operator;

12. The Hotel is open for business and Operator is operating the Hotel;

13. There are no actions, whether voluntary or otherwise, pending against Operator under the bankruptcy, reorganization, or similar laws of the United States, any state thereof, or any other jurisdiction.

14. The term of the Agreement commenced on _ _[*date*]_ _, and shall expire on _ _[*date*]_ _, unless sooner terminated in accordance with the terms of the Agreement. Operator has no option to renew or extend the term, except as set forth below: _ _[*Describe options to renew or extend; if none, insert "None"*]_ _;

15. Operator has no option or right to purchase all or any part of the Hotel.

16. A true and correct copy of the Monthly Report for the Hotel for the last month for which such monthly report has been completed is attached to this Estoppel.

17. A true and correct copy of the Operating Plan and Budget for _ _[____]_ _ as prepared by Operator for the Hotel is attached to this Estoppel.

The foregoing statements are accurate to the best of Operator's knowledge. Operator acknowledges and agrees that Buyer and Lender shall be entitled to rely on Operator's certifications set forth herein.

IN WITNESS WHEREOF, Operator has executed this instrument on _ _[*date*]_ _.

OPERATOR: _ _[*Name of entity*]_ _,
a _ _[*specify type of entity*]_ _

By: __[*Signature*]__
Name: _ _[*Typed name*]_ _
Title: _____

© The Regents of the University of California

Appendix S

Escrow Instructions—General Provisions



GENERAL PROVISIONS

IMPORTANT – PLEASE READ CAREFULLY

1. Privacy Notice (15 U.S.C. 6801 and 16 CFR Part 313)

We collect nonpublic personal information about you from information you provide on forms and documents and from other people such as your lender, real estate agent, attorney, title company, etc. We do not disclose any nonpublic personal information about our customers or former customers to anyone, except as permitted by law. We restrict access to nonpublic personal information about you to those employees who need to know that information in order to provide products or services to you. We maintain physical, electronic and procedural safeguards that comply with federal regulations to guard your nonpublic personal information.

2. Execution & Delivery of Escrow Instructions

These instructions may be executed in counterparts and said counterparts together will constitute one and the same instrument. In the event that the parties hereto utilize facsimile or electronically transmitted instructions to Escrow Holder, said parties hereby instruct Escrow Holder to rely upon such instructions as if they were originals. Any amendments and supplements to these instructions must be in writing and shall only be effective when executed and delivered to Escrow Holder. Escrow Holder shall not be concerned with nor have any obligations with respect to items designated as memoranda in these instructions or with any other agreement or contract between the parties to this escrow.

3. Deposit of Funds

(i) All funds received in this escrow will be deposited with other escrow funds in one or more non-interest-bearing escrow accounts of Escrow Holder in a financial institution selected by Escrow Holder. Escrow Holder shall not be responsible and shall have no liability for any delay in closing this escrow if the funds deposited in this escrow are not available for immediate withdrawal as a matter of right following deposit in such financial institution.

(ii) You have the opportunity to earn interest on the funds you deposit with us through a deposit account arrangement that Escrow Holder has established with one of its financial institutions. The interest rate for these accounts varies between financial institutions, fluctuates periodically based on market conditions and other factors, and may change prior to or during the time your funds are on deposit. You will not have an opportunity to earn interest on any funds deposited by a lender.

(iii) If you elect to earn interest through this special account arrangement, Escrow Holder will charge you an additional fee of $35.00 for the establishment and maintenance of the account. This fee compensates Escrow Holder for the costs associated with opening and managing the interest-bearing account, preparing correspondence/documentation, transferring funds, maintaining appropriate records for audit/reconciliation purposes and filing any required tax withholding statements. It is important that you consider this cost in your decision since the cost may exceed the interest you earn. If you are interested in having your funds deposited in an interest-bearing account, please contact your escrow officer.

(iv) If you do not elect to have your funds deposited in an interest-bearing account, your funds (together with any funds deposited by a lender) will be held in Escrow Holder's general escrow trust account. The general escrow trust account is restricted and protected against claims by third parties or creditors of Escrow Holder. Escrow Holder and/or its parent company may receive certain direct and indirect financial benefits from the financial institution as a result of maintaining the general escrow trust account. These benefits may include, without limitation, credits allowed by such financial institution on loans to Escrow Holder and/or its parent company and earnings on investments made with the proceed of such loans, as well as accounting, reporting and other services and products of such financial institution. Escrow Holder shall have no obligation to account to the parties to this escrow in any manner for the value of, or to pay to any party, any benefit received by Escrow Holder and/or its parent company. Any such benefits shall be deemed additional compensation of Escrow Holder for its services in connection with this escrow. Some or all of these benefits may be deemed interest due you under California Insurance Code Section 12413.5. As indicated above, you may elect to have your funds placed in a separate, interest-bearing account and receive the benefits therefrom, but you will be required to pay Escrow Holder an additional fee for this service. Alternatively, you may leave your funds in the general escrow

trust account and thereby authorize Escrow Holder to keep the benefits it and/or its parent company receives from the financial institution. In either event, you understand and agree that Escrow Holder and/or its parent company may receive and retain for their sole benefit any and all benefits derived from the general escrow trust account prior to the deposit of your funds in an interest-bearing account and following the withdrawal of your funds from such interest-bearing account (normally two business days prior to the close of escrow).

(v) All parties depositing funds in connection with this escrow are hereby notified that the funds so deposited are insured only to the limit provided by the Federal Deposit Insurance Corporation.

(vi) Funds deposited by a lender are ordinarily deposited to escrow one or two days prior to closing. You should be aware that your lender may begin charging interest on your loan from the date loan funds are deposited into Escrow Holder's escrow trust account.

4. Good Funds Law – California Insurance Code §12413.1

All parties are aware and understand that California Insurance Code §12413.1 mandates that funds deposited into an escrow must be collected and available for withdrawal PRIOR TO DISBURSEMENT. The determination of the availability of funds is set forth as follows:

(i) CASH AND ELECTRONIC TRANSFERS ("wired funds") are available for SAME DAY disbursement.

(ii) CASHIER'S CHECKS AND CERTIFIED CHECKS are available for disbursement THE NEXT BUSINESS DAY;

In order to avoid unnecessary delays of two to seven days, or more, please use wire transfers, cashier's checks or certified checks whenever possible.

5. License of Escrow Holder

Escrow Holder is licensed by the California Department of Insurance to act as an underwritten title company, or if Escrow Holder's name includes the word "Insurance", Escrow Holder has a Certificate of Authority issued by the California Department of Insurance to transact the business of title insurance.

6. Prorations

All adjustments and prorations called for in this escrow shall be made on the basis of a thirty (30) day month, unless otherwise instructed in writing.

7. Sufficiency, Validity, Authority, etc. of Documents

Escrow Holder shall not be responsible or have any liability with respect to the sufficiency or correctness as to form, manner of execution, or validity of any document deposited in this escrow, nor as to the identity, authority or rights of any person executing the same. Escrow Holder's duties hereunder shall be limited to the proper handling and disbursement of funds deposited in this escrow and the proper safekeeping and delivery of such documents received by Escrow Holder, in accordance with the written instructions given to Escrow Holder in this escrow in which all parties have concurred.

8. Conveyance and Vesting

Escrow Holder is instructed to draw a Grant Deed, using any standard form, conveying title from Seller to Buyer, with Buyer's legal vesting. Buyer acknowledges that Escrow Holder cannot give advice as to vesting, and understands that the vesting designated may have significant legal and tax consequences. Buyer is advised to seek the advice of Buyer's own attorney and accountant with regard to vesting. Buyer shall furnish Escrow Holder with Buyer's vesting prior to the date of preparation of Buyer's loan documents or close of escrow (if Buyer is not obtaining financing). Escrow Holder is hereby authorized and instructed to complete and/or correct Buyer's vesting on the Grant Deed, even if it has already been executed and notarized. If Buyer is married and taking title alone, (1) Buyer shall furnish Escrow Holder with the name of Buyer's spouse, (2) Escrow Holder is authorized and instructed to prepare an Interspousal Transfer or Quitclaim Deed for Buyer's spouse's signature and (3) Escrow Holder is to record same at close of escrow, charging Buyer's account for the preparation and recording fees associated with this deed.

Print

9. Copies of Escrow Instructions

Escrow Holder is authorized to furnish copies of these instructions, any supplements and/or amendments thereto, notices of cancellation and closing statements to any real estate brokers or agents representing any party to this escrow and to any lender whose loan will be paid through this escrow or will be used to fund this escrow.

10. Cancellation

In the event this escrow is canceled, the parties hereto agree to pay Escrow Holder its cancellation fee for work performed, and to pay all expenses incurred by Escrow Holder. If a demand to cancel this escrow is submitted to Escrow Holder or if there is no written communication from the parties for a period of six months, Escrow Holder shall notify the parties of its intention to cancel this escrow and return all documents and funds (less cancellation fees and costs) to the party depositing the same. If no written objection to such notice is given to Escrow Holder within fifteen (15) days of mailing such notice, Escrow Holder shall cancel this escrow and return all funds and/or documents then held by Escrow Holder to the party depositing the same.

11. Disputes

No notice, demand or change of instruction shall be of any effect in this escrow unless given in writing by all parties affected thereby. In the event a demand for funds and/or documents deposited with Escrow Holder in connection with this escrow is made and which is not concurred in by all parties hereto, Escrow Holder, notwithstanding which party made such demand, may elect to do any of the following:

(i) Take no further action in connection with this escrow and continue to hold such funds and/or documents until receipt of mutual concurring instructions from all parties to this escrow as to the disposition of such funds and/or documents;

(ii) Commence an action in interpleader and obtain an order from the court allowing Escrow Holder to deposit such funds and/or documents with the court, in which case Escrow Holder shall have no further liability or obligations with respect to this escrow; or

(iii) In the event that any party commences an action against any other party with respect to this escrow, deposit such funds and/or documents with the court, in which case Escrow Holder shall have no further liability or obligations with respect to this escrow.

In the event Escrow Holder interpleads any funds and/or documents with any court pursuant to either subparagraphs (ii) or (iii) above, Escrow Holder shall be entitled to reimbursement of its reasonable attorneys' fees and expenses of litigation in connection with such action.

12. Arbitration

In the event of a claim or controversy between Escrow Holder and any party hereto involving an amount greater than $5,000.00 and arising out of this escrow, either Escrow Holder or such other party may demand arbitration pursuant to the Rules of the American Arbitration Association. The decision of the arbitrator shall be binding on all parties and judgment upon the award of the arbitrator may be entered in any court having jurisdiction thereof.

13. No Duty to Notify as to Other Transactions

Escrow Holder shall have no duty or responsibility to notify any party to this escrow of any sale, resale, loan, exchange or other transaction involving the property which is the subject of this escrow or any profit realized by any person or entity in connection therewith, notwithstanding that Escrow Holder may act as escrow holder for such transaction(s) in this or another escrow(s).

14. Failure to Close Timely

If the conditions for closing this escrow have not occurred at the time set forth herein for closing, Escrow Holder is nevertheless to continue to act hereunder and to close this escrow as soon thereafter as such conditions (except as to time) shall have been met, unless any party shall have made a written demand on Escrow Holder for cancellation of this escrow and/or for the return of any funds and/or documents deposited by such party.

Print

15. Delivery of Documents and Funds

All documents and funds due the parties to this escrow will be sent by Escrow Holder via regular mail to the parties at the addresses provided to Escrow Holder, unless otherwise instructed. Delivery by escrow holder of documents to a party's real estate agent or broker shall constitute delivery to that party.

16. Retention of Records

After the closing or cancellation of this escrow and the disbursement of all funds and recording and/or delivery of all documents in accordance with the written instructions given to Escrow Holder in this escrow, Escrow Holder is authorized to destroy or otherwise dispose of its file(s) with respect to this escrow without notice or liability to the parties hereto.

17. California Withholding (APPLIES TO SALES THAT OCCUR BEFORE JANUARY 1, 2003)

In accordance with California Revenue and Taxation Code §18662, a Buyer may be required to withhold an amount equal to 3-1/3 percent of the sales price in the case of a disposition of a California real property interest by either:

1. A seller who is an individual with a last known street address outside of California or when the disbursement instructions authorize the proceeds to be sent to a financial intermediary of Seller, OR

2. A corporate seller which has no permanent place of business in California.

Buyer may become subject to penalty for failure to withhold an amount equal to the greater of 10 percent of the amount required to be withheld or five hundred dollars ($500).

However, notwithstanding any other provision included in the California statutes referenced above, no buyer will be required to withhold any amount or be subject to penalty for failure to withhold if:

1. The sales price of the California real property conveyed does not exceed one hundred thousand dollars ($100,000), OR

2. Seller executes a written certificate, under the penalty of perjury, certifying that Seller is a resident of California, or if a corporation, has a permanent place of business in California, OR

3. Seller, who is an individual, executes a written certificate, under the penalty of perjury, that the California real property being conveyed is Seller's principal residence (as defined in Section 1034 of the Internal Revenue Code).

Seller is subject to penalty for knowingly filing a fraudulent certificate for the purpose of avoiding the withholding requirement.

The California statutes referenced above include provisions which authorize the Franchise Tax Board to grant reduced withholding and waivers from withholding on a case-by-case basis.

Buyer understands that in no event will Escrow Holder undertake to advise Buyer and/or Buyer's representative on the possible application of the above code sections to this specific transaction. Unless expressly instructed by Seller and Buyer herein, Buyer understands that Escrow Holder will NOT assist in obtaining a waiver from withholding from the Franchise Tax Board.

Should Buyer and Seller herein direct Escrow Holder to undertake any activities pursuant to the withholding provisions under California law, Buyer and Seller agree to cooperate fully in providing necessary information to Escrow Holder. Buyer and Seller agree to indemnify and hold Escrow Holder harmless in the event of noncompliance resulting from information supplied by either Buyer and/or Seller. For additional information concerning the withholding provisions under the code sections referenced above, please contact the Franchise Tax Board-Withhold-at-Source Unit at (916) 845-4900, P.O. Box 651, Sacramento, CA 95812-0651.

17. California Withholding (APPLIES TO SALES THAT OCCUR ON OR AFTER JANUARY 1, 2003)

In accordance with Section 18662 of the Revenue and Taxation Code, a buyer may be required to withhold an amount equal to 31/3 percent of the sales price in the case of a disposition of California real property interest by either:

1. A seller who is an individual or when the disbursement instructions authorize the proceeds to be sent to a financial intermediary of the seller, OR

2. A corporate seller that has no permanent place of business in California.

The buyer may become subject to penalty for failure to withhold an amount equal to the greater of 10 percent of the amount required to be withheld or five hundred dollars ($500).

However, notwithstanding any other provision included in the California statutes referenced above, no buyer will be required to withhold any amount or be subject to penalty for failure to withhold if:

1. The sales price of the California real property conveyed does not exceed one hundred thousand dollars ($100,000), OR

2. The seller executes a written certificate, under the penalty of perjury, certifying that the seller is a corporation with a permanent place of business in California, OR

3. The seller, who is an individual, executes a written certificate, under the penalty of perjury, of any of the following:

A. That the California real property being conveyed is the seller's principal residence (within the meaning of Section 121 of the Internal Revenue Code).

B. That the California real property being conveyed is or will be exchanged for property of like kind (within the meaning of Section 1031 of the Internal Revenue Code), but only to the extent of the amount of gain not required to be recognized for California income tax purposes under Section 1031 of the Internal Revenue Code.

C. That the California real property has been compulsorily or involuntarily converted (within the meaning of Section 1033 of the Internal Revenue Code) and that the seller intends to acquire property similar or related in service or use so as to be eligible for nonrecognition of gain for California income tax purposes under Section 1033 of the Internal Revenue Code.

D. That the California real property transaction will result in a loss for California income tax purposes.

The seller is subject to penalty for knowingly filing a fraudulent certificate for the purpose of avoiding the withholding requirement.

The California statutes referenced above include provisions which authorize the Franchise Tax Board to grant reduced withholding and waivers from withholding on a case-by-case basis for corporations or other entities.

Buyer understands that in no event will Escrow Holder undertake to advise Buyer and/or Buyer's representative on the possible application of the above code sections to this specific transaction. Unless expressly instructed by Seller and Buyer herein, Buyer understands that Escrow Holder will NOT assist in obtaining a waiver from withholding from the Franchise Tax Board.

Should Buyer and Seller herein direct Escrow Holder to undertake any activities pursuant to the withholding provisions under California law, Buyer and Seller agree to cooperate fully in providing necessary information to Escrow Holder. Buyer and Seller agree to indemnify and hold Escrow Holder harmless in the event of noncompliance resulting from information supplied by either Buyer and/or Seller. For additional information concerning the withholding provisions under the code sections referenced above, please contact the Franchise Tax Board-Withhold-at-Source Unit at (916) 845-4900, P.O. Box 651, Sacramento, CA 95812-0651.

18. Foreign Investment in Real Property Act (FIRPTA)

Buyer is hereby notified that FIRPTA withholding (Internal Revenue Code Section 1445) may be applicable to certain sales of United States real estate by non-resident aliens. Unless instructed otherwise by the parties to this escrow, Escrow Holder is released from any liability, obligation or responsibility with respect to compliance with said Code Section, including, but not limited to (a) withholding of funds, (b) advising the parties as to the requirements of said sections, (c) determining whether transferor (Seller) is a foreign person or entity and/or (d) obtaining a non-foreign affidavit.

19. Preliminary Change of Ownership

Prior to the close of escrow, Buyer may hand Escrow Holder a fully completed and executed "Preliminary Change of Ownership Report" (PCOR) pursuant to the requirements of California Revenue and Taxation Code Section 480.3. Buyer may elect not to complete and execute said form prior to the close of escrow. Should Buyer choose not to execute the PCOR or should the County Recorders office reject the PCOR for any reason, Buyer is aware that a $20.00 charge will be assessed by the County Recorder's office and Escrow Holder will

charge the account of Buyer accordingly. In the event the PCOR has not been filed at the time the documents record OR the County Tax Assessors office determines that the form has not been properly completed, Buyer will be responsible for obtaining and completing a new PCOR and any additional documents that may be required by the Assessor's office. Failure to file a proper PCOR will result in additional penalties in accordance with Section 480 of the California Revenue and Taxation Code. Escrow Holder's sole duty shall be the delivery of the PCOR to the County Recorder at the time of recordation of transfer documents, if it is provided to Escrow Holder. Escrow Holder assumes no liability or responsibility regarding the proper completion of the PCOR.

20. Supplemental Taxes

Buyer is advised that the County Tax Assessor will revalue property that changes ownership or contains new construction, which may result in a supplemental assessment. The supplemental taxes will be assessed from the date of the change in ownership or completion of construction.

21. Fire/Hazard Insurance

Buyer shall obtain Fire/Hazard Insurance coverage on the subject property prior to the close of escrow, as per requirements of the new lender. If Buyer has not paid policy premium prior to close of escrow, Escrow Holder is authorized and instructed to debit Buyer's account with the cost of the annual premium and pay such premium to the insurance agent and/or company, at the close of escrow, from funds deposited by Buyer. Escrow Holder is instructed to request that the insurance company deliver the original policy and copies, as required, to all necessary parties. In the event the property is covered by a blanket insurance policy, Buyer shall provide Escrow Holder with a Certificate of Insurance. FAILURE TO PROVIDE FIRE/HAZARD INSURANCE WILL DELAY THE CLOSE OF ESCROW. Escrow Holder has no obligation to obtain fire or other insurance in the absence of a written instruction to do so.

22. Fees and Charges; Messenger Fees

Escrow, title, and recording charges and other costs are to be charged to the principals' accounts in accordance with customary practices in this County, unless Escrow Holder is instructed to do otherwise in writing. The charges which the Company will make for sending documents and/or checks via next day messenger services (i.e. Federal Express, UPS, DHL, Airborne, Express Mail, etc.) are $15.00 per letter, standard overnight service, and $25.00 for larger size packages and/or priority delivery services. Such charges include the cost of such messenger service and the Company's expenses for arranging such messenger service and its overhead and profit. Special messenger services will be billed at the cost of such services. There will be no additional charge for pick-up or delivery of packages via the Company's regularly scheduled messenger runs.

23. Fees Paid in Advance

Escrow Holder is hereby instructed to use Buyer's funds deposited into escrow to pay any fees required prior to close of escrow to entities such as, but not limited to, homeowner's association management companies for ordering documents and statements, lenders for ordering payoff statements, and cities which require city reports. In the event escrow is cancelled and Buyer is entitled to a refund of deposited funds, the amount of any fees advanced shall be deducted from the funds returned to Buyer. Seller hereby agrees to immediately deposit into escrow the amount of fees advanced for which Seller is responsible, and Escrow Holder will immediately disburse the amount of such deposit to Buyer. Buyer hereby agrees to immediately return to Escrow Holder any documentation provided to Buyer that is associated with fees advanced by Escrow Holder. Buyer shall not be reimbursed for any fees associated with documents provided to Buyer which are not returned to Escrow Holder. Escrow Holder shall not be liable to Buyer for fees deducted from Buyer's deposit in the event Seller fails to deposit the amount of such fees into escrow.

24. Special Recording; Late Confirmation of Recording

Seller's proceeds may not be available, and encumbrances may not be paid off, until the first business day following the day of recording if 1) documents recorded at close of escrow are recorded later in the day than 8:00 a.m. (which is called a "special recording") or if 2) the County Recorder does not provide confirmation of recording within sufficient time to allow same-day disbursement of funds by wire or check.

25. IRS Form 1099 Requirements

If requested by Escrow Holder, Seller will furnish Escrow Holder with sufficient information to file form 1099, if required, with the Internal Revenue Service for the sale of the real property which is subject to this escrow.

Print

26. Disclosure Reports

Escrow holder is not to be concerned with disclosures made by the parties to each other. In the event escrow holder receives any disclosure reports requiring signatures or approval by a party, escrow holder's only responsibility will be to forward the report to the appropriate party.

27. Loan Payoffs

When a mortgage, deed of trust or tax lien is to be paid off through escrow, Escrow holder is authorized to pay the payoff demand received from the creditor. Seller/borrower understands that a loan payoff may include a prepayment penalty and other charges.

© The Regents of the University of California

Appendix T

Real Estate Withholding—Computation of Estimated Gain or Loss (FTB Form 593-E)



YEAR **2008**

Real Estate Withholding — Computation of Estimated Gain or Loss

CALIFORNIA FORM **593-E**

(You are required to complete this form if you claim an exemption due to a loss or zero gain or if you elect an optional gain on sale withholding amount.)

Name	Seller or Transferor: ☐ SSN or ITIN ☐ FEIN ☐ CA Corp. No.
Address (including suite, room, PO Box, or PMB no.)	
City / State / ZIP Code	
Property address (if not street address, provide parcel number and county)	

1 **Selling price** ..... 1 _____

2 Selling expenses ..... 2 _____

3 **Amount Realized.** Subtract line 2 from line 1 ..... 3 _____

4 Enter the price you paid to purchase the property (If you acquired the property other than by purchase, see page 9, Table 1 to determine your basis.) ..... 4 _____

5 Seller-paid points ..... 5 _____

6 Depreciation ..... 6 _____

7 Other decreases to basis ..... 7 _____

8 Total decreases to basis. Add line 5 through line 7 ..... 8 _____

9 Subtract line 8 from line 4 ..... 9 _____

10 Cost of additions and improvements ..... 10 _____

11 Other increases to basis ..... 11 _____

12 Total increases to basis. Add line 10 and line 11 ..... 12 _____

13 **Adjusted basis.** Add line 9 and line 12 ..... 13 _____

14 Enter any suspended passive activity losses from this property ..... 14 _____

15 Add line 13 and line 14 ..... 15 _____

16 **Estimated Gain or Loss on Sale.** Subtract line 15 from line 3 and enter the amount here. If you have a loss or zero gain, skip lines 17 and 18. Complete the Seller's Signature area below and check the Yes box on Form 593-C, line 3. If you have a gain, go to line 17 ..... 16 _____

17 **Optional Gain on Sale Withholding Amount.** Check the applicable box for the filing type.

☐ Individual 9.3% ☐ Corporation 8.84% ☐ Bank and Financial Corporation 10.84%

☐ S Corporation 1.5% ☐ Financial S Corporation 3.5%

Multiply the amount on line 16 by the tax rate for the filing type selected above and enter the result on line 17. This is the optional gain on sale withholding amount.

If you elect the optional gain on sale withholding amount on line 17, check the appropriate box on line 4 (Boxes B-F) for the Optional Gain on Sale Election on Form 593, and transfer the amount on line 17 to Form 593, line 5. Sign Form 593 to certify the election ..... 17 _____

18 **Total Sales Price Withholding Amount.** Multiply the selling price on line 1 by 3 1/3% (.0333) and enter the amount on line 18. This is the total sales price withholding amount.

If you select the **total sales price withholding amount** on line 18, check Box A "**3 1/3% (.0333) x Total Sales Price**" on line 4 of Form 593, and transfer the amount on line 18 to Form 593, line 5 ..... 18 _____

Seller's Signature

Title and escrow persons and exchange accommodators are not authorized to provide legal or accounting advice for purposes of determining withholding amounts. Transferors are strongly encouraged to consult with a competent tax professional for this purpose.

Under penalties of perjury, I hereby certify that the information provided above is, to the best of my knowledge, true and correct. I understand that I must retain this form in my records for 5 years and that the Franchise Tax Board may review relevant escrow documents to ensure withholding compliance and if conditions change, I will promptly inform the withholding agent. I understand that completing this form does not exempt me from filing a California income tax return to report this sale.

Seller's Name (type or print) _____

Seller's Signature _____ Date: _____

Spouse's/RDP's Name (if jointly owned) _____

Spouse's/RDP's Signature (if jointly owned) _____ Date: _____

© The Regents of the University of California

Source: Real Property/California Real Property Sales Transactions/Appendix U Real Estate Withholding Certificate (FTB Form 593-C)

Appendix U

Real Estate Withholding Certificate (FTB Form 593-C)



YEAR

CALIFORNIA FORM

2008 Real Estate Withholding Certificate

593-C

Part I – Seller's Information **Return this form to your escrow company.**

Name (including spouse/RDP, if jointly owned - see instructions - type or print)	☐ SSN or ITIN ☐ FEIN ☐ CA Corp no.
Address (including suite, room, PO Box, or PMB no.)	Spouse's/RDP's SSN or ITIN (if jointly owned)

City	State	ZIP Code	Ownership Percentage
			%

Property address (if no street address, provide parcel number and county)

Read the following and check the appropriate boxes. (See line-by-line notes in the instructions).

Part II – Certifications which fully exempt the sale from withholding: **YES** **NO**

1. Does the property qualify as the seller's (or decedent's, if being sold by the decedent's estate) **principal residence** within the meaning of Internal Revenue Code (IRC) Section 121? ☐ ☐
2. Did the seller (or decedent, if being sold by the decedent's estate) last use the property as the seller's (decedent's) principal residence within the meaning of IRC Section 121 without regard to the two-year time period? ☐ ☐
3. Will the seller have a loss or zero gain for California income tax purposes on this sale? (To check YES, you must complete Form 593-E, Real Estate Withholding — Computation of Estimated Gain or Loss, and have a loss or zero gain on line 16). ☐ ☐
4. Is the property being compulsorily or involuntarily converted and does the seller intend to acquire property that is similar or related in service or use to qualify for nonrecognition of gain for California income tax purposes under IRC Section 1033? ☐ ☐
5. Will the transfer qualify for nonrecognition treatment under IRC Section 351 (transfer to a corporation controlled by the transferor) or IRC Section 721 (contribution to a partnership in exchange for a partnership interest)? ☐ ☐
6. Is the seller a corporation (or an LLC classified as a corporation for federal and California income tax purposes) that is either qualified through the California Secretary of State or has a permanent place of business in California? ☐ ☐
7. Is the seller a partnership (or an LLC that is classified as a partnership for federal and California income tax purposes and is not a disregarded single member LLC) with recorded title to the property in the name of the partnership or LLC? (If yes, the partnership or LLC must withhold on nonresident partners or members as required). ☐ ☐
8. Is the seller a tax-exempt entity under either California or federal law? ☐ ☐
9. Is the seller an insurance company, individual retirement account, qualified pension/profit sharing plan, or charitable remainder trust? ☐ ☐

Part III – Certifications that may partially or fully exempt the sale from withholding:

Real Estate Escrow Person: See instructions for amounts to withhold.

10. Will the transfer qualify as a simultaneous like-kind exchange within the meaning of IRC Section 1031? ☐ ☐
11. Will the transfer qualify as a deferred like-kind exchange within the meaning of IRC Section 1031? ☐ ☐
12. Will the transfer of this property be an installment sale that you will report as such for California tax purposes **and** has the buyer agreed to withhold on each principal payment instead of withholding the full amount at the time of transfer? ☐ ☐

Part IV – Seller's Signature

Under penalties of perjury, I hereby certify that the information provided above is, to the best of my knowledge, true and correct. If conditions change, I will promptly inform the withholding agent. I understand that the Franchise Tax Board may review relevant escrow documents to ensure withholding compliance and that completing this form does **not** exempt me from filing a California income or franchise tax return to report this sale.

Seller's Name and Title _____ Seller's Signature _____ Date _____

Spouse's/RDP's Name _____ Spouse's/RDP's Signature _____ Date _____

Please verify that the SSN or ITIN listed above in Part I of this form is correct.

Seller: If you checked **YES** to **any** question in Part II, you are exempt from real estate withholding.
If you checked **YES** to **any** question in Part III, you may qualify for a partial or complete withholding exemption.
If you checked **NO** to **all** of the questions in Part II and Part III, the withholding will be 3⅓% (.0333) of the total sales price or the optional gain on sale withholding amount certified by seller on Form 593.
If you are withheld upon, the withholding agent should give you one copy of Form 593, Real Estate Withholding Tax Statement. Attach a copy to the lower front of your California income tax return and make a copy for your records.

You should keep Form 593-C for five years following the close of the transaction. You must furnish the form to the FTB upon request.

© The Regents of the University of California

Appendix V

Real Estate Withholding Installment Sale Agreement (FTB Form 593-I)



YEAR **2008**

Real Estate Withholding Installment Sale Agreement

(This form can only be completed by the buyer. This is not a remittance document.)

CALIFORNIA FORM **593-I**

Part I – Buyer's Information **Return this form to your real estate escrow person.**

Name			SSN or ITIN – –
Spouse's/RDP's Name (if jointly purchased)			Spouse's/RDP's SSN or ITIN (if jointly purchased) – –
Address (including apt./suite, room, PO Box, or PMB no.)			☐ FEIN ☐ CA Corp no.
City	State	ZIP Code –	Daytime telephone number ( ) –
Property address (if no street address, provide parcel number and county)			

Part II – Seller's Information

Name			SSN or ITIN – –
Spouse's/RDP's Name (if jointly purchased)			Spouse's/RDP's SSN or ITIN (if jointly owned) – –
Address (including apt./suite, room, PO Box, or PMB no.)			☐ FEIN ☐ CA Corp no.
City	State	ZIP Code –	Installment Withholding Percent ___ ___ . ___ ___% Apply this percent to all installment payments.

Part III – Installment Agreement

Attach to Form 593-I a copy of the signed promissory note (showing the installment payment requirement). If the seller has elected and certified the Optional Gain on Sale withholding amount, also attach an executed copy of seller's certification of Form 593, Real Estate Withholding Tax Statement, to Form 593-I.

Part IV – Buyer's Agreement to Withhold (Be sure to read the "Buyer" information below before you sign.)

Under penalties of perjury, I hereby agree to withhold on the principal portion of each installment payment for the above shown California real property to the above seller at the rate of 3⅓% or the Optional Gain on Sale withholding percentage, as specified by the seller on Form 593, of the principal portion of each installment payment. I will complete Form 593, Real Estate Withholding Tax Statement, for the principal portion of each installment payment and send one copy of each to the Franchise Tax Board along with the withholding payment, and give one copy of Form 593 to the seller. I will send each withholding payment to the Franchise Tax Board by the 20th day of the month following the month of the installment payment. If the terms of the installment sale, promissory note, or payment schedule change, I will promptly inform the Franchise Tax Board. I understand that the Franchise Tax Board may review relevant escrow documents to ensure withholding compliance. I also understand that completing and signing this form will subject me to withholding penalties if I do not withhold on the principal portion of each installment payment and do not send the withholding along with Form 593 to the Franchise Tax Board by the due date, or if I do not send one copy of Form 593 to the seller by the due date.

Buyer's name (if the buyer is not an individual, buyer's agent's name and title) (type or print) _____

Buyer's signature _____ Date: _____

Buyer's spouse's/RDP's name (if on title) _____

Buyer's spouse's/RDP's signature (if applicable) _____ Date: _____

Buyer: **If you sign this agreement**, make a copy of this form. Make sure you copy both sides so you will have the instructions for withholding on subsequent payments. Give the original along with copies of the promissory note and seller's certified Form 593 to your real estate escrow person who should mail them in to the Franchise Tax Board. Your real estate escrow person will withhold on the first installment payment. You must withhold on **all** subsequent installment payments (including payoff or balloon payments). Do not complete this form unless you are willing to either withhold 3 1/3% or the Optional Gain on Sale withholding percentage, as specified by the seller on Form 593, for each installment payment. Complete Form 593, and mail the documents and payment to the FTB for the principal portion of each installment payment.

This agreement is between the buyer and the Franchise Tax Board. Neither the seller nor the buyer may modify the terms of the agreement.

If you choose not to sign this agreement, instruct your real estate escrow person to withhold either the full 3⅓% of the total sales price or the Optional Gain on Sale withholding amount certified by the seller on Form 593. You will not be required to withhold on subsequent installment payments.

Real Estate Escrow Person: If this form is completed and signed, withhold only on the first installment payment in escrow. Make a copy of this form for your records. Attach the original Form 593-I, a copy of the promissory note, and seller's certified Form 593, and send to the Franchise Tax Board with the withholding payment.

© The Regents of the University of California

Appendix W

FIRPTA Certification



Commonwealth
A LANDAMERICA COMPANY

FIRPTA CERTIFICATION

To: **Commonwealth Land Title Company**
777 Arnold Drive, 1st Floor
Martinez, CA 94553
Phone: **(925) 335-3300** Fax: **(925) 957-9940**

Escrow Officer: **Marilynne McDuffey**

Escrow No.: **MCDUFFEY-MM1**
Date:

Property Address:
123 Main Street
Windsor, CA 94553

SECTION 1445 of the Internal Revenue Code provides that a Transferee of a U.S. real property interest must withhold tax if the Transferor is a foreign person. This Certification is provided by Sally Sample, an unmarried woman and Mary Cline, a single woman and John E. Smith and June A. Smith, husband and wife and Trevor Dillon and Natalie Dillon, husband and wife and Santos, Mateo, a California corporation and Haley Vaughn Santos, husband and wife (SELLER) to ABC Company, a California corporation, a single man (BUYERS) in connection with sale of that certain real property by Seller to Buyer. To inform Buyer that withholding of tax is not required by disposition of a U.S. real property interest by Seller, the undersigned hereby certifies the following on behalf of Seller:

1. Seller is not a non-resident alien, foreign corporation, foreign partnership, foreign trust, or foreign estate (as those terms are defined in the Internal Revenue Code and Income Tax Regulations);
2. Seller's U.S. Employer Identification Number/Social Security Number is: _____; and
3. Seller's home address is: _____
_____

The undersigned Seller understands that this Certification may be disclosed to the Internal Revenue Service by Transferee and that any false statement contained herein could be punished by fine, imprisonment, or both.

UNDER PENALTIES OF PERJURY, I declare that I have examined this Certification and to the best of my knowledge believe it is true, correct and complete.

Dated and Effective as of: _____

SELLER(S) SIGNATURE(S):

_____ _____
Sally Sample Mary Cline

_____ _____
John E. Smith June A. Smith

Each of the above parties states that they have read the foregoing instructions and understands and agree to them.

© The Regents of the University of California

Appendix X

Buyers/Borrowers Estimated Closing Statement



OMB Approval No. 2502-0265

Good Faith Estimate (GFE)

Name of Originator	Borrower
Originator Address	Property Address
Originator Phone Number	
Originator Email	Date of GFE

Purpose

This GFE gives you an estimate of your settlement charges and loan terms if you are approved for this loan. For more information, see HUD's *Special Information Booklet* on settlement charges, your *Truth-in-Lending Disclosures*, and other consumer information at www.hud.gov/respa. If you decide you would like to proceed with this loan, contact us.

Shopping for your loan

Only you can shop for the best loan for you. Compare this GFE with other loan offers, so you can find the best loan. Use the shopping chart on page 3 to compare all the offers you receive.

Important dates

1. The interest rate for this GFE is available through _____. After this time, the interest rate, some of your loan Origination Charges, and the monthly payment shown below can change until you lock your interest rate.
2. This estimate for all other settlement charges is available through _____.
3. After you lock your interest rate, you must go to settlement within ____ days (your rate lock period) to receive the locked interest rate.
4. You must lock the interest rate at least ____ days before settlement.

Summary of your loan

Your initial loan amount is	$
Your loan term is	years
Your initial interest rate is	%
Your initial monthly amount owed for principal, interest, and any mortgage insurance is	$ per month
Can your interest rate rise?	☐ No ☐ Yes, it can rise to a maximum of %. The first change will be in
Even if you make payments on time, can your loan balance rise?	☐ No ☐ Yes, it can rise to a maximum of $
Even if you make payments on time, can your monthly amount owed for principal, interest, and any mortgage insurance rise?	☐ No ☐ Yes, the first increase can be in and the monthly amount owed can rise to $. The maximum it can ever rise to is $.
Does your loan have a prepayment penalty?	☐ No ☐ Yes, your maximum prepayment penalty is $
Does your loan have a balloon payment?	☐ No ☐ Yes, you have a balloon payment of $ due in years.

Escrow account information

Some lenders require an escrow account to hold funds for paying property taxes or other property related charges in addition to your monthly amount owed of $_____.
Do we require you to have an escrow account for your loan?
☐ No, you do not have an escrow account. You must pay these charges directly when due.
☐ Yes, you have an escrow account. It may or may not cover all of these charges. Ask us.

Summary of your settlement charges

A	Your Adjusted Origination Charges *(See page 2)*	$
B	Your Charges for All Other Settlement Services *(See page 2)*	$
A + B	Total Estimated Settlement Charges	$

Print

Understanding your estimated settlement charges

Your Adjusted Origination Charges

1. Our origination charge This charge is for getting this loan for you.	
2. Your credit or charge (points) for the specific interest rate chosen ☐ The credit or charge for the interest rate of [ ] % is included in "Our origination charge." (See item 1 above.) ☐ You receive a credit of $[ ] for this interest rate of [ ] %. This credit **reduces** your settlement charges. ☐ You pay a charge of $[ ] for this interest rate of [ ] %. This charge (points) **increases** your total settlement charges. The tradeoff table on page 3 shows that you can change your total settlement charges by choosing a different interest rate for this loan.	
A Your Adjusted Origination Charges	$

Some of these charges can change at settlement. See the top of page 3 for more information.

Your Charges for All Other Settlement Services

3. Required services that we select These charges are for services we require to complete your settlement. We will choose the providers of these services. *Service* — *Charge*	
4. Title services and lender's title insurance This charge includes the services of a title or settlement agent, for example, and title insurance to protect the lender, if required.	
5. Owner's title insurance You may purchase an owner's title insurance policy to protect your interest in the property.	
6. Required services that you can shop for These charges are for other services that are required to complete your settlement. We can identify providers of these services or you can shop for them yourself. Our estimates for providing these services are below. *Service* — *Charge*	
7. Government recording charges These charges are for state and local fees to record your loan and title documents.	
8. Transfer taxes These charges are for state and local fees on mortgages and home sales.	
9. Initial deposit for your escrow account This charge is held in an escrow account to pay future recurring charges on your property and includes ☐ all property taxes, ☐ all insurance, and ☐ other [ ].	
10. Daily interest charges This charge is for the daily interest on your loan from the day of your settlement until the first day of the next month or the first day of your normal mortgage payment cycle. This amount is $[ ] per day for [ ] days (if your settlement is [ ]).	
11. Homeowner's insurance This charge is for the insurance you must buy for the property to protect from a loss, such as fire. *Policy* — *Charge*	
B Your Charges for All Other Settlement Services	$
A + B Total Estimated Settlement Charges	$

Print

Instructions

Understanding which charges can change at settlement

This GFE estimates your settlement charges. At your settlement, you will receive a HUD-1, a form that lists your actual costs. Compare the charges on the HUD-1 with the charges on this GFE. Charges can change if you select your own provider and do not use the companies we identify. (See below for details.)

These charges **cannot increase** at settlement:	The total of these charges **can increase up to 10%** at settlement:	These charges **can change** at settlement:
▪ Our origination charge ▪ Your credit or charge (points) for the specific interest rate chosen *(after you lock in your interest rate)* ▪ Your adjusted origination charges *(after you lock in your interest rate)* ▪ Transfer taxes	▪ Required services that we select ▪ Title services and lender's title insurance *(if we select them or you use companies we identify)* ▪ Owner's title insurance *(if you use companies we identify)* ▪ Required services that you can shop for *(if you use companies we identify)* ▪ Government recording charges	▪ Required services that you can shop for *(if you do not use companies we identify)* ▪ Title services and lender's title insurance *(if you do not use companies we identify)* ▪ Owner's title insurance *(if you do not use companies we identify)* ▪ Initial deposit for your escrow account ▪ Daily interest charges ▪ Homeowner's insurance

Using the tradeoff table

In this GFE, we offered you this loan with a particular interest rate and estimated settlement charges. However:

- If you want to choose this same loan with **lower settlement charges,** then you will have a **higher interest rate.**
- If you want to choose this same loan with a **lower interest rate,** then you will have **higher settlement charges.**

If you would like to choose an available option, you must ask us for a new GFE.

Loan originators have the option to complete this table. Please ask for additional information if the table is not completed.

	The loan in this GFE	The same loan with lower settlement charges	The same loan with a lower interest rate
Your initial loan amount	$	$	$
Your initial interest rate[1]	%	%	%
Your initial monthly amount owed	$	$	$
Change in the monthly amount owed from this GFE	No change	You will pay $ **more** every month	You will pay $ **less** every month
Change in the amount you will pay at settlement with this interest rate	No change	Your settlement charges will be **reduced** by $	Your settlement charges will **increase** by $
How much your total estimated settlement charges will be	$	$	$

[1] *For an adjustable rate loan, the comparisons above are for the initial interest rate before adjustments are made.*

Using the shopping chart

Use this chart to compare GFEs from different loan originators. Fill in the information by using a different column for each GFE you receive. By comparing loan offers, you can shop for the best loan.

	This loan	Loan 2	Loan 3	Loan 4
Loan originator name				
Initial loan amount				
Loan term				
Initial interest rate				
Initial monthly amount owed				
Rate lock period				
Can interest rate rise?				
Can loan balance rise?				
Can monthly amount owed rise?				
Prepayment penalty?				
Balloon payment?				
Total Estimated Settlement Charges				

If your loan is sold in the future

Some lenders may sell your loan after settlement. Any fees lenders receive in the future cannot change the loan you receive or the charges you paid at settlement.

© The Regents of the University of California

Appendix Y

Settlement Statement



OMB Approval No. 2502-0265

A. Settlement Statement (HUD-1)

B. Type of Loan			
1. ☐ FHA 2. ☐ RHS 3. ☐ Conv. Unins. 4. ☐ VA 5. ☐ Conv. Ins.	6. File Number:	7. Loan Number:	8. Mortgage Insurance Case Number:

C. Note: This form is furnished to give you a statement of actual settlement costs. Amounts paid to and by the settlement agent are shown. Items marked "(p.o.c.)" were paid outside the closing; they are shown here for informational purposes and are not included in the totals.

D. Name & Address of Borrower:	E. Name & Address of Seller:	F. Name & Address of Lender:
G. Property Location:	H. Settlement Agent: Place of Settlement:	I. Settlement Date:

J. Summary of Borrower's Transaction		K. Summary of Seller's Transaction	
100. Gross Amount Due from Borrower		**400. Gross Amount Due to Seller**	
101. Contract sales price		401. Contract sales price	
102. Personal property		402. Personal property	
103. Settlement charges to borrower (line 1400)		403.	
104.		404.	
105.		405.	
Adjustment for items paid by seller in advance		**Adjustments for items paid by seller in advance**	
106. City/town taxes to		406. City/town taxes to	
107. County taxes to		407. County taxes to	
108. Assessments to		408. Assessments to	
109.		409.	
110.		410.	
111.		411.	
112.		412.	
120. Gross Amount Due from Borrower		**420. Gross Amount Due to Seller**	
200. Amounts Paid by or in Behalf of Borrower		**500. Reductions In Amount Due to Seller**	
201. Deposit or earnest money		501. Excess deposit (see instructions)	
202. Principal amount of new loan(s)		502. Settlement charges to seller (line 1400)	
203. Existing loan(s) taken subject to		503. Existing loan(s) taken subject to	
204.		504. Payoff of first mortgage loan	
205.		505. Payoff of second mortgage loan	
206.		506.	
207.		507.	
208.		508.	
209.		509.	
Adjustments for items unpaid by seller		**Adjustments for items unpaid by seller**	
210. City/town taxes to		510. City/town taxes to	
211. County taxes to		511. County taxes to	
212. Assessments to		512. Assessments to	
213.		513.	
214.		514.	
215.		515.	
216.		516.	
217.		517.	
218.		518.	
219.		519.	
220. Total Paid by/for Borrower		**520. Total Reduction Amount Due Seller**	
300. Cash at Settlement from/to Borrower		**600. Cash at Settlement to/from Seller**	
301. Gross amount due from borrower (line 120)		601. Gross amount due to seller (line 420)	
302. Less amounts paid by/for borrower (line 220)	( )	602. Less reductions in amount due seller (line 520)	( )
303. Cash ☐ **From** ☐ **To Borrower**		**603. Cash** ☐ **To** ☐ **From Seller**	

The Public Reporting Burden for this collection of information is estimated at 35 minutes per response for collecting, reviewing, and reporting the data. This agency may not collect this information, and you are not required to complete this form, unless it displays a currently valid OMB control number. No confidentiality is assured; this disclosure is mandatory. This is designed to provide the parties to a RESPA covered transaction with information during the settlement process.

Print

L. Settlement Charges

700. Total Real Estate Broker Fees				Paid From Borrower's Funds at Settlement	Paid From Seller's Funds at Settlement
Division of commission (line 700) as follows					
701. $	to				
702. $	to				
703. Commission paid at settlement					
704.					

800. Items Payable in Connection with Loan				
801. Our origination charge		$	(from GFE #1)	
802. Your credit or charge (points) for the specific interest rate chosen		$	(from GFE #2)	
803. Your adjusted origination charges			(from GFE A)	
804. Appraisal fee to			(from GFE #3)	
805. Credit report to			(from GFE #3)	
806. Tax service to			(from GFE #3)	
807. Flood certification			(from GFE #3)	
808.				

900. Items Required by Lender to Be Paid in Advance				
901. Daily interest charges from	to	@ $	/day	(from GFE #10)
902. Mortgage insurance premium	for	months to		(from GFE #3)
903. Homeowner's insurance	for	years to		(from GFE #11)
904.				

1000. Reserves Deposited with Lender				
1001. Initial deposit for your escrow account			(from GFE #9)	
1002. Homeowner's insurance	months @ $	per month	$	
1003. Mortgage insurance	months @ $	per month	$	
1004. Property taxes	months @ $	per month	$	
1005.	months @ $	per month	$	
1006.	months @ $	per month	$	
1007. Aggregate Adjustment			-$	

1100. Title Charges				
1101. Title services and lender's title insurance			(from GFE #4)	
1102. Settlement or closing fee			$	
1103. Owner's title insurance			(from GFE #5)	
1104. Lender's title insurance			$	
1105. Lender's title policy limit $				
1106. Owner's title policy limit $				
1107. Agent's portion of the total title insurance premium			$	
1108. Underwriter's portion of the total title insurance premium			$	

1200. Government Recording and Transfer Charges				
1201. Government recording charges			(from GFE #7)	
1202. Deed $	Mortgage $	Releases $		
1203. Transfer taxes			(from GFE #8)	
1204. City/County tax/stamps	Deed $	Mortgage $		
1205. State tax/stamps	Deed $	Mortgage $		
1206.				

1300. Additional Settlement Charges			
1301. Required services that you can shop for		(from GFE #6)	
1302.		$	
1303.		$	
1304.			
1305.			

1400. Total Settlement Charges (enter on lines 103, Section J and 502, Section K)		

Print

Comparison of Good Faith Estimate (GFE) and HUD-1 Charges		Good Faith Estimate	HUD-1
Charges That Cannot Increase	**HUD-1 Line Number**		
Our origination charge	# 801		
Your credit or charge (points) for the specific interest rate chosen	# 802		
Your adjusted origination charges	# 803		
Transfer taxes	#1203		

Charges That in Total Cannot Increase More Than 10%		Good Faith Estimate	HUD-1
Government recording charges	# 1201		
	#		
	#		
	#		
	#		
	#		
	#		
	#		
Total			
Increase between GFE and HUD-1 Charges		**$** **or** **%**	

Charges That Can Change				Good Faith Estimate	HUD-1
Initial deposit for your escrow account	#1001				
Daily interest charges	# 901	$	/day		
Homeowner's insurance	# 903				
	#				
	#				
	#				

Loan Terms

Your initial loan amount is	$
Your loan term is	years
Your initial interest rate is	%
Your initial monthly amount owed for principal, interest, and and any mortgage insurance is	$ includes ☐ Principal ☐ Interest ☐ Mortgage Insurance
Can your interest rate rise?	☐ No. ☐ Yes, it can rise to a maximum of %. The first change will be on and can change again every after . Every change date, your interest rate can increase or decrease by %. Over the life of the loan, your interest rate is guaranteed to never be **lower** than % or **higher** than %.
Even if you make payments on time, can your loan balance rise?	☐ No. ☐ Yes, it can rise to a maximum of $.
Even if you make payments on time, can your monthly amount owed for principal, interest, and mortgage insurance rise?	☐ No. ☐ Yes, the first increase can be on and the monthly amount owed can rise to $. The maximum it can ever rise to is $.
Does your loan have a prepayment penalty?	☐ No. ☐ Yes, your maximum prepayment penalty is $.
Does your loan have a balloon payment?	☐ No. ☐ Yes, you have a balloon payment of $ due in years on .
Total monthly amount owed including escrow account payments	☐ You do not have a monthly escrow payment for items, such as property taxes and homeowner's insurance. You must pay these items directly yourself. ☐ You have an additional monthly escrow payment of $ that results in a total initial monthly amount owed of $. This includes principal, interest, any mortgage insurance and any items checked below: ☐ Property taxes ☐ Homeowner's insurance ☐ Flood insurance ☐ ☐ ☐

Note: If you have any questions about the Settlement Charges and Loan Terms listed on this form, please contact your lender.

Print

ESCROW FILE NUMBER: MCDUFFEY-999 MM1 OMB No. 2502-0265

BREAKDOWN OF PAYOFF ON HUD line 505

Payoff to: Beneficial Loan #:

Description	Amount
Principal Balance	25,000.00
Interest from 01/01/2002 to 01/04/2002	29.79
Late Fees	88.12
Prepayment Fees	2,500.00
Statement Fees	50.00
escrow overdraft	1,456.00
prorated mortgage ins.	45.50
Reconveyance fee	65.00
Total Payoff	29,234.41

Payoff to: Beneficial Loan #:

Description	Amount
trustees fees	200.00
fax fee	15.00
Total Payoff	215.00

Total as shown on HUD line #505. **29,449.41**

Print

Attachments:

BREAKDOWN OF NEW LOANS

Description	Buyer Amount	Seller Amount
, , , Loan#		
, , , Loan#		
Total of New Loans.	**0.00**	

HUD 900 ITEMS REQUIRED BY LENDER TO BE PAID IN ADVANCE

Description	Buyer Amount	Seller Amount
906. aggregrate	(550.00)	
Total as shown on HUD Page 2 Line #905.	**(550.00)**	

HUD 1100 BREAKDOWN OF TITLE CHARGES

Description	Buyer Amount	Seller Amount
Owners Policy $ 500,000.00	700.00	
Lenders Policy $ 1,800,000.00	1,200.00	
Lenders Policy $ 50,000.00	250.00	
1115. ends. fee to Commonwealth Land Title Company	100.00	
1116. Central Signing Service fee to Commonwealth Land Title Company	100.00	
Total as shown on HUD Page 2 Line #1113.	**2,350.00**	

© The Regents of the University of California

Appendix Z

Supplemental Escrow Instructions—Funds Held



LandAmerica Commonwealth

777 Arnold Drive, 1st Floor
Martinez, CA 94553
Phone: (925) 335-3300
Fax: (925) 957-9940

SUPPLEMENTAL ESCROW INSTRUCTIONS – FUNDS HELD

To: **Commonwealth Land Title Company**
777 Arnold Drive, 1st Floor
Martinez, CA 94553
Phone: **(925) 335-3300** Fax: **(925) 957-9940**

Escrow Officer:

Escrow No.: Property Address:
Date:

Commonwealth Land Title Company, hereinafter called escrow holder, is hereby authorized and instructed to hold the sum of $____ at the close of escrow from proceeds due the undersigned seller. Said funds are to be held for the following purpose:

Escrow holder shall have no obligation to inspect any repairs. Upon submission of bills to escrow holder by ____ which have been marked "approved" and initialed by the parties herein, escrow holder is authorized to pay said "approved" bills, without any liability of the authenticity of said bills, and refund any balance held to the undersigned SELLER.

In the event escrow holder has not received "approved" bills within ____ from close of escrow, or the amount held is insufficient to cover said bills, escrow holder is authorized, but not obligated, to disburse all funds held to BUYER WITHOUT FURTHER INSTRUCTIONS. Escrow holder shall not be held liable for any bill or group of bills presented individually or collectively in excess of the amount held.

It is acknowledged that escrow holder may not make disbursements for each bill, but that a complete set of bills shall be assembled by the parties and submitted at one time, at which time all disbursements and/or refunds shall be made. The undersigned agree that the extent of escrow holder's obligation is to receive and disburse monies in the manner set for the above, and escrow shall have no other obligations.

The undersigned agree that there may be a service charge of $25.00 per month for administering said funds. Said service charge may be deducted from said funds for each and every calendar month or any portion thereof during which said funds are held.

ANY MODIFICATION OF THIS INSTRUCTION SHALL BE GIVEN MUTUALLY BY SELLER AND BUYER IN WRITING **PRIOR TO CLOSE OF ESCROW** AND ESCROW HOLDER IS SPECIFICALLY INSTRUCTED THAT ONLY SUCH MUTUAL INSTRUCTIONS ARE TO BE RECOGNIZED.

If conflicting instructions are given to escrow holder, escrow holder may hold any undisbursed monies until the rights of the parties are determined by court action, or escrow holder may interplead in accordance with the General Provisions of the escrow instructions.

The undersigned hereby indemnify and hold escrow holder harmless against all costs, damages, attorneys' fees, expenses and liabilities which escrow holder may incur or sustain in connection with these instructions, or any court action arising therefrom, and will pay the same upon demand.

Print

SELLER(S) SIGNATURE(S):

_____	_____ DATE	_____	_____ DATE
_____	_____ DATE	_____	_____ DATE

BUYER(S) SIGNATURE(S):

_____	_____ DATE	_____	_____ DATE
_____	_____ DATE	_____	_____ DATE

Received and acknowledged:

Commonwealth Land Title Company

By: _____ Date Received: _____

© The Regents of the University of California

Appendix AA

Escrow Cancellation Instructions



LandAmerica Commonwealth

777 Arnold Drive, 1st Floor
Martinez, CA 94553
Phone: (925) 335-3300
Fax: (925) 957-9940

CANCELLATION INSTRUCTIONS

To: **Commonwealth Land Title Company**
777 Arnold Drive, 1st Floor
Martinez, CA 94553
Phone: **(925) 335-3300** Fax: **(925) 957-9940**

Escrow Officer:

Escrow No.:
Date:

Property Address:

You are hereby instructed to cancel the above numbered escrow upon your receipt of this instruction executed by all parties named below.

You are to disburse Buyer's deposit in the amount of $___ as follows:

☐ Seller ☐ Buyer

☐_____

Upon receipt of this instruction executed by all parties hereto and the disbursement of funds as set forth hereinabove, you are to consider this escrow cancelled and of no further force or effect. You are to return any original documents in your possession to the parties who deposited same.

You, as Escrow Holder, are relieved of any and all liability and will be held harmless for failure of this escrow to close.

Each of the above parties states that they have read the above instructions and understands and agree to them.

SELLER(S) SIGNATURE(S):

_____ _____

_____ _____

BUYER(S) SIGNATURE(S):

_____ _____

_____ _____

Print

LISTING REAL ESTATE BROKER

By:_____ _____
Date

License No.: $

Address:
Telephone:

SELLING REAL ESTATE BROKER

By:_____ _____
Date

License No.: $

Address:
Telephone:

© The Regents of the University of California

Appendix BB

Preliminary Change of Ownership Report



BOE-502-A (FRONT) REV. 10 (8-07)

PRELIMINARY CHANGE OF OWNERSHIP REPORT

FOR RECORDER'S USE ONLY

[To be completed by transferee (buyer) prior to transfer of subject property in accordance with section 480.3 of the Revenue and Taxation Code.] A Preliminary Change of Ownership Report must be filed with each conveyance in the County Recorder's office for the county where the property is located; this particular form may be used in all 58 counties of California.

THIS REPORT IS NOT A PUBLIC DOCUMENT

SELLER/TRANSFEROR:

BUYER/TRANSFEREE:

ASSESSOR'S PARCEL NUMBER(S)

PROPERTY ADDRESS OR LOCATION:

MAIL TAX INFORMATION TO: Name

Address

NOTICE: A lien for property taxes applies to your property on January 1 of each year for the taxes owing in the following fiscal year, July 1 through June 30. One-half of these taxes is due November 1, and one-half is due February 1. The first installment becomes delinquent on December 10, and the second installment becomes delinquent on April 10. One tax bill is mailed before November 1 to the owner of record. **You may be responsible for the current or upcoming property taxes even if you do not receive the tax bill.**

The property which you acquired may be subject to a supplemental assessment in an amount to be determined by the _____ Assessor. For further information on your supplemental roll obligation, please call the _____ Assessor at _____.

PART I: TRANSFER INFORMATION *(please answer all questions)*

YES	NO	
☐	☐	A. Is this transfer solely between husband and wife (addition of a spouse, death of a spouse, divorce settlement, etc.)?
☐	☐	B. Is this transaction only a correction of the name(s) of the person(s) holding title to the property (for example, a name change upon marriage)? Please explain _____
☐	☐	C. Is this document recorded to create, terminate, or reconvey a lender's interest in the property?
☐	☐	D. Is this transaction recorded only as a requirement for financing purposes or to create, terminate, or reconvey a security interest (e.g., cosigner)? Please explain _____
☐	☐	E. Is this document recorded to substitute a trustee of a trust, mortgage, or other similar document?
☐	☐	F. Did this transfer result in the creation of a joint tenancy in which the seller (transferor) remains as one of the joint tenants?
☐	☐	G. Does this transfer return property to the person who created the joint tenancy (original transferor)?
		H. Is this a transfer of property:
☐	☐	1. to a revocable trust that may be revoked by the transferor and is for the benefit of the ☐ transferor ☐ transferor's spouse?
☐	☐	2. to a trust that may be revoked by the Creator/Grantor who is also a joint tenant, and which names the other joint tenant(s) as beneficiaries when the Creator/Grantor dies?
☐	☐	3. to an irrevocable trust for the benefit of the ☐ Creator/Grantor and/or ☐ Grantor's spouse?
☐	☐	4. to an irrevocable trust from which the property reverts to the Creator/Grantor within 12 years?
☐	☐	I. If this property is subject to a lease, is the remaining lease term 35 years or more including written options?
☐	☐	*J. Is this a transfer between ☐ parent(s) and child(ren)? ☐ or from grandparent(s) to grandchild(ren)?
☐	☐	*K. Is this transaction to replace a principal residence by a person 55 years of age or older? Within the same county? ☐ Yes ☐ No
☐	☐	*L. Is this transaction to replace a principal residence by a person who is severely disabled as defined by Revenue and Taxation Code section 69.5? Within the same county? ☐ Yes ☐ No
☐	☐	M. Is this transfer solely between domestic partners currently registered with the California Secretary of State?

*If you checked yes to J, K or L, you may qualify for a property tax reassessment exclusion, which may result in lower taxes on your property. **If you do not file a claim, your property will be reassessed.**

Please provide any other information that will help the Assessor to understand the nature of the transfer.

If the conveying document constitutes an exclusion from a change in ownership as defined in section 62 of the Revenue and Taxation Code for any reason other than those listed above, set forth the specific exclusions claimed: _____.

Please answer all questions in each section. If a question does not apply, indicate with "N/A." Sign and date at bottom of second page.

PART II: OTHER TRANSFER INFORMATION

A. Date of transfer if other than recording date _____

B. Type of transfer *(please check appropriate box)*:

☐ Purchase ☐ Foreclosure ☐ Gift ☐ Trade or Exchange ☐ Merger, Stock, or Partnership Acquisition

☐ Contract of Sale — Date of Contract _____

☐ Inheritance — Date of Death _____ ☐ Other *(please explain)*: _____

☐ Creation of Lease ☐ Assignment of a Lease ☐ Termination of a Lease ☐ Sale/Leaseback

☐ Date lease began _____

☐ Original term in years (including written options) _____

☐ Remaining term in years (including written options) _____

Monthly Payment _____ Remaining Term _____

C. Was only a partial interest in the property transferred? ☐ Yes ☐ No

If **yes**, indicate the percentage transferred _____%.

Print

Please write Assessor's Parcel Number(s): _____

Please answer, to the best of your knowledge, all applicable questions, then sign and date. If a question does not apply, indicate with "N/A."

PART III: PURCHASE PRICE AND TERMS OF SALE

A. CASH DOWN PAYMENT OR value of trade or exchange *(excluding closing costs)* Amount $_____

B. FIRST DEED OF TRUST @ _____ % interest for _____ years. Pymts./Mo. = $_____ (Prin. & Int. only) Amount $_____
- ☐ FHA(_____ Discount Points) ☐ Fixed rate ☐ New loan
- ☐ Conventional ☐ Variable rate ☐ Assumed existing loan balance
- ☐ VA (_____ Discount Points) ☐ All inclusive D.T. ($ _____ Wrapped) ☐ Bank or savings & loan
- ☐ Cal-Vet ☐ Loan carried by seller ☐ Finance company

Balloon payment ☐ Yes ☐ No Due Date _____ Amount $ _____

C. SECOND DEED OF TRUST @ _____ % interest for _____ years. Pymts./Mo. = $_____ (Prin. & Int. only) Amount $_____
- ☐ Bank or savings & loan ☐ Fixed rate ☐ New loan
- ☐ Loan carried by seller ☐ Variable rate ☐ Assumed existing loan balance

Balloon payment ☐ Yes ☐ No Due Date _____ Amount $ _____

D. OTHER FINANCING: Is other financing involved not covered in (b) or (c) above? ☐ Yes ☐ No Amount $_____

Type _____ @ _____ % interest for _____ years. Pymts./Mo. = $_____ (Prin. & Int. only)
- ☐ Bank or savings & loan ☐ Fixed rate ☐ New loan
- ☐ Loan carried by seller ☐ Variable rate ☐ Assumed existing loan balance

Balloon payment ☐ Yes ☐ No Due Date _____ Amount $ _____

E. WAS AN IMPROVEMENT BOND ASSUMED BY THE BUYER? ☐ Yes ☐ No Outstanding Balance: Amount $_____

F. TOTAL PURCHASE PRICE *(or acquisition price, if traded or exchanged, include real estate commission if paid)*
TOTAL ITEMS A THROUGH E $

G. PROPERTY PURCHASED ☐ Through a broker ☐ Direct from seller ☐ From a family member ☐ Other *(please explain):* _____

If purchased through a broker, provide broker's name and phone number: _____

Please explain any special terms, seller concessions, or financing and any other information that would help the Assessor understand the purchase price and terms of sale: _____

PART IV: PROPERTY INFORMATION

A. TYPE OF PROPERTY TRANSFERRED:
- ☐ Single-family residence
- ☐ Multiple-family residence (no. of units: _____)
- ☐ Commercial/Industrial
- ☐ Other (Description: i.e., timber, mineral, water rights, etc. _____)
- ☐ Agricultural
- ☐ Co-op/Own-your-own
- ☐ Condominium
- ☐ Timeshare
- ☐ Manufactured home
- ☐ Unimproved lot

B. IS THIS PROPERTY INTENDED AS YOUR PRINCIPAL RESIDENCE? ☐ Yes ☐ No
If **yes**, enter date of occupancy _____ (month) / _____ (day), 20 _____ (year) or intended occupancy _____ (month) / _____ (day), 20 _____ (year)

C. IS PERSONAL/BUSINESS PROPERTY INCLUDED IN PURCHASE PRICE (i.e., furniture, farm equipment, machinery, etc.) (other than a manufactured home subject to local property tax)? ☐ Yes ☐ No
If **yes**, enter the value of the personal/business property included in the purchase price $ _____ *(Must attach itemized list.)*

D. IS A MANUFACTURED HOME INCLUDED IN PURCHASE PRICE? ☐ Yes ☐ No
If **yes**, how much of the purchase price is allocated to the manufactured home? _____
Is the manufactured home subject to local property tax? ☐ Yes ☐ No What is the decal number? _____

E. DOES THE PROPERTY PRODUCE INCOME? ☐ Yes ☐ No If **yes**, is the income from:
☐ Lease/Rent ☐ Contract ☐ Mineral rights ☐ Other *(please explain):* _____

F. WHAT WAS THE CONDITION OF THE PROPERTY AT THE TIME OF SALE?
☐ Good ☐ Average ☐ Fair ☐ Poor

Please explain the physical condition of the property and provide any other information (such as restrictions, etc.) that would assist the Assessor in determining the value of the property:

CERTIFICATION

OWNERSHIP TYPE (☑)
- Proprietorship ☐
- Partnership ☐
- Corporation ☐
- Other _____ ☐

I certify that the foregoing is true, correct and complete to the best of my knowledge and belief. This declaration is binding on each and every co-owner and/or partner.

NAME OF NEW OWNER/CORPORATE OFFICER		TITLE
SIGNATURE OF NEW OWNER/CORPORATE OFFICER ▶		DATE
NAME OF ENTITY *(typed or printed)*		FEDERAL EMPLOYER ID NUMBER
ADDRESS *(typed or printed)*	PHONE NUMBER (8 a.m. - 5 p.m.)	E-MAIL ADDRESS *(optional)*

(Note: The Assessor may contact you for additional information.)
If a document evidencing a change of ownership is presented to the recorder for recordation without the concurrent filing of a preliminary change of ownership report, the recorder may charge an additional recording fee of twenty dollars ($20).

© The Regents of the University of California

Directory

NOTE: For a discussion of Internet use by attorneys, online terminology, and a comprehensive list of Internet sites, see Internet Law and Practice in California (Cal CEB 2004).

§1.3:

To obtain a copy of Profile of Legal Malpractice Claims: 2004-2007, American Bar Association Standing Committee on Lawyers' Professional Liability, contact the ABA Service Center. The phone number of the ABA Service Center is (800) 285-2221. The address is 321 North Clark Street, Chicago, IL 60654. Alternatively, search the Web Store at the ABA website: http://www.abanet.org.

§1.4:

The State Bar's Ethics Hotline is (415) 538-2150. An "800" number is available in California: (800) 2-ETHICS.

§1.19:

Sample fee agreements are available from the State Bar's website at http://www.calbar.ca.gov or by writing to Mandatory Fee Arbitration Program, State Bar of California, 180 Howard Street, San Francisco, CA 94105-1639.

§§1.86, 4.93:

On the California State Budget, see the website of the California Department of Finance: http://www.dof.ca.gov.

§§1.122-1.124, 1.126-1.130:

Third-Party Legal Opinion Report, Including the Legal Opinion Accord, of the Section of Business Law, American Bar Association, published in 47 Bus Law, 167 (Nov. 1991), is available for purchase from the American Bar Association, Service Center, 321 North Clark Street, Chicago, IL 60654. See the ABA's website at http://www.abanet.org.

The publications California Opinion Reports (2002), *Legal Opinions in Business Transactions* (2005 Report), including the 2007 update to the Report on Third Party Remedies, and various other State Bar reports are available on the State Bar's website, http://www.calbar.ca.gov.

Business Law Section of the State Bar of California Report on the Third-Party Legal Opinion Report of the ABA Section of Business Law (May 1992) is available for purchase from the Business Law Section of the State Bar of California, 180 Howard Street, San Francisco, CA 94105-1639. See the State Bar's website at http://www.calbar.ca.gov.

§§2.2, 2.171:

The website for the California Department of Real Estate is http://www.dre.ca.gov.

§2.12A:

To request an interpretive opinion under Bus & P C §10236, write to the Department of Real Estate at 2201 Broadway, Sacramento, CA 95818-2500, Attn: Chief Counsel.

§2.17:

The website for the State of California Employment Development Department is http://www.edd.cahwnet.gov.

§2.175:

To purchase a copy of the Code of Ethics and Standards of Practice or the Interpretations of the Code of Ethics, call the National Association of REALTORS® at (800) 874-6500, or search the website: http://www.realtor.org. The website for the California Association of REALTORSÒ is http://www.car.org.

§4.25:

A form of Certificate of Limited Partnership (LP-1) may be found on the website of the California Secretary of State: http://www.sos.ca.gov.

§4.49:

For more information about the Energy Star program, go to http://www.energystar.gov.

§4.62:

Instructions on how to apply for a Certificate of Discharge of Property From Federal Tax Lien may be found on the Internal Revenue Service's website at http://www.irs.gov. Updated lien payoff amounts can be requested by calling the IRS at (800) 913-6050.

§§4.79, 6.76:

Certified copies of pest control inspection reports can be obtained from the Structural Pest Control Board for a nominal fee. Call (800) PEST-188 or write 2005 Evergreen Street, Ste 1500, Sacramento, CA 95815. The Board's website is http://www.pestboard.ca.gov.

§4.81:

Type of Natural Hazard Area/Zone	Responsible Agency	Source of Information
Special flood hazard area (Zone A or Zone V)	FEMA	FEMA (800) 621-FEMA www.FEMA.gov/hazard/flood
Area of potential flooding	State Office of Emergency Services (OES), Department of Water Resources	OES (916) 845-8510 www.oes.ca.gov
Very high fire hazard severity zone	State Department of Forestry and Fire Protection	Fire and Resource Assessment Program (916) 327-3939 www.frap.cdf.ca.gov
Wildlands fire area	State Department of Forestry and Fire Protection	Fire and Resource Assessment Program (916) 327-3939 www.frap.cdf.ca.gov
Earthquake fault zone	California Geological Survey www.conservation.ca.gov/cgs	BPS Reprographic Service (415) 512-6550
Seismic hazard zone	California Geological Survey www.conservation.ca.gov/cgs	BPS Reprographic Services 945 Bryant St., San Francisco, CA 94103 (415) 512-6550

The State Resources Agency has a natural hazard disclosure statement home page that has a list of resources available for all six natural hazard zones. The Internet address of the home page is http://ceres.ca.gov/planning/nhd. The address is 1416 Ninth Street #1311, Sacramento, CA 95814; (916) 653-5656

§4.119:

The website for the Department of the Treasury, Office of Foreign Assets Control (OFAC), is http://www.treas.gov/offices/enforcement/ofac.

§6.35:

The website for JCP Geologists is http://www.disclosures.com, and for Property ID is http://www.propertyid.com.

§6.58:

The publication *Guidelines for Earthquake Bracing of Residential Water Heaters* is available on the State Architect's website, http://www.dsa.dgs.ca.gov/.

§6.67:

Mortgagee Letters are available from the Department of Housing and Urban Development (HUD) on its Client Information and Policy System website at http://www.hud.gov/offices/adm/hudclips.

§§7.27, 7.29, 7.37:

The website for the American Society for Testing and Materials is http://www.astm.org.

§§11.17, 11.93:

The website for information regarding the next edition of the Bureau of Land Management, Manual of Instructions for the Survey of the Public Lands of the United States is http://www.blm.gov/wo/st/en/prog/more/cadastralsurvey/next_edition.html.

§§13.33, 14.2:

The website for the Insurance Services Office (ISO) is http://www.iso.com. Only members of the ISO can obtain ISO forms and policies from the website; they are also available on Lexis.

§13.52:

The website for the California Earthquake Authority (CEA) is http://www.earthquakeauthority.com.

§13.124:

The website for the American Association of Insurance Services (AAIS) is http://www.aaisonline.com.

§13.130:

The Dwelling Policy can be found at the FEMA website: http://www.fema.gov.

§13.137:

The Consumer Product Safety Commission has posted information on Chinese Drywall on the CPSC website: http://www.cpsc.gov/info/drywall/index.html.

§14.46:

Discussion of the additional changes to the 2007 CGL policy is available on the International Risk Management Institute's website at http://www.irmi.com.

§15.76:

The website for the Franchise Tax Board is http://www.ftb.ca.gov.

§15.84:

The website for the Internal Revenue Service is http://www.irs.gov.

© The Regents of the University of California

Table of Statutes, Regulations, and Rules

CALIFORNIA

Constitution

Art XI, §5: §6.95
Art XI, §7: §1.77
Art XIII, §8: §4.93
Art XIIIA: §10.34
Art XV, §1: §§2.9, 9.6

Statutes

BUSINESS AND PROFESSIONS CODE

125.6: §2.181
480(a): §2.171
490: §2.171
6076: §1.4
6106.3: §2.8B
6125: §2.147
6147: §1.19
6147(b): §1.19
6148: §1.19
6148(c): §1.19
7195-7199: §6.77
7195(a)(1): §6.77
7195(a)(2): §6.77
7195(b): §6.77
7195(c): §6.77
7196: §6.77
7197(a): §6.77
7197(b): §6.77
7198: §6.77
7199: §6.77
8500-8697.5: §6.76
8506.1: §6.76
8507: §6.76
8516: §6.59
8516(b): §6.76
8516(b)(9)-(10): §6.76
8516(b)(13): §6.76
8516(c)(1)-(2): §6.76
8516(d): §6.76
8516(e): §6.76
8516(i): §6.76
8516.5: §6.76
8518: §6.76
8519: §6.76
8519(b): §4.79
8731: §11.8
8741(b): §11.8
8762-8771.5: §11.24
10000-10580: §§2.1, 2.8A, 2.149, 2.164-2.165, 2.171-2.174, 2.176, 2.178, 2.181
10008.5: §2.10
10026: §2.8B
10030: §2.10
10032: §§2.15-2.16, 2.20
10071: §2.171
10081: §2.174

10084.1: §6.54
10085: §2.8B
10085.6: §2.8B
10086: §2.174
10100: §2.173
10100.2: §2.173
10101: §2.173
10130: §§2.2, 2.91, 2.174
10131: §§2.2, 2.6, 2.8B, 2.10
10131(a): §2.2
10131(d): §§2.2, 2.7
10131(e): §2.2
10131.1: §§2.2, 2.6, 2.8B
10131.1(b)(1)(B): §2.2
10131.1(b)(1)(C): §2.2
10131.2: §2.2
10131.3: §2.11
10132: §§2.13-2.14
10133: §2.6
10133(a): §2.6
10133.1: §2.6
10133.1(11): §2.8B
10133.1(b): §2.2
10136: §2.94
10137: §§2.13-2.14, 2.21, 2.167
10137.1: §2.4
10138: §§2.167, 15.94
10139: §2.2
10140: §2.12
10140.5-10140.6: §2.12
10142: §§2.43, 2.88
10145: §§2.42, 2.67, 2.70, 2.149
10146: §2.149
10147: §§4.81, 6.52
10147.5: §§2.55, 2.79, 2.118
10147.6: §2.8B
10149: §6.52
10150: §2.91
10150.6: §2.3
10151(d): §2.3
10153: §§2.3-2.4, 2.145
10153.2: §2.3
10153.3-10153.5: §§2.3, 2.145
10158: §2.4
10159.5: §2.4
10160: §2.14
10161.8: §2.21
10167: §2.118
10170-10171.5: §2.145
10170.5(a)(4): §2.181
10175: §2.173
10175-10176: §2.174
10175-10185: §2.152
10175.2: §2.174
10176-10177: §§2.65, 2.171
10176(a): §2.135
10176(d): §2.129
10176(e): §2.149
10176(f): §§2.56, 2.58-2.59, 2.63
10176(g): §§2.61, 2.131, 2.135
10176(i): §§2.176, 4.135
10176(k)-(*l*): §2.171
10177: §§2.8B, 2.18, 2.88, 2.118, 2.174
10177-10177.4: §2.171
10177(f): §2.171

10177(h): §§2.14, 2.179
10177(j): §§2.3, 2.171
10177(*l*): §2.181
10177(o): §4.135
10177(p): §2.4
10177(q): §2.8B
10177(r): §2.8B
10177.1: §2.173
10177.4: §§2.5, 2.135
10177.5: §2.15
10177.6: §2.31
10185: §2.174
10211: §2.4
10235.5: §2.12
10236: §2.12A, Directory
10236.4: §2.12
10240: §6.69
10240-10241: §2.8
10240-10248.3: §§2.7-2.8, 2.8B
10240(a): §2.8
10240(b): §2.8
10240(c): §2.8
10240.1: §2.8
10242(a): §2.8
10242.6: §§9.30, 9.45
10245: §2.8
10246.6: §9.45
10248.3: §2.8
10450.6: §§2.164, 2.174
10470-10481: §2.164
10471: §§2.164-2.166
10471 (former): §2.167
10471(a): §§2.164, 2.167
10471(c)(7)(E): §2.170
10471(c)(7)(F): §2.168
10471(d): §2.167
10471.1-10472: §2.170
10471.5(c): §2.170
10472(a): §2.170
10473: §2.166
10474: §2.169
10474(d): §2.169
10474.5: §2.169
10475: §2.170
11000-11200: §§9.104, 15.4
11010: §6.49
11010.4: §§6.35, 6.47
11013.1: §9.104
11013.2: §9.104
11018.1: §6.35
11018.1(c): §6.63
11018.6: §§6.60, 6.63
11210-11288: §5.7
11423(b): §9.12
11423(g): §9.12
11535 (former): §9.103
16600-17365: §2.41
16700-16770: §§2.41, 2.118
17000-17101: §13.98
17200: §§13.122-13.123
17200-17210: §13.122
17203: §13.122
17206: §13.122
17500: §2.12
17511-17511.13: §2.12

17530: §2.12
17536(a): §2.12
17538.43: §2.12
17538.45: §2.12
17539.4: §2.12
17900-17930: §14.33
23000-25762: §5.22
24074: §5.22
24076: §5.22

CIVIL CODE
14: §§4.7, 10.59
18-19: §4.151
18(1): §15.86
19: §§6.73, 11.11, 11.16, 11.48, 12.2, 15.86
38: §4.16
39: §4.16
40: §§4.16, 10.76
51: §§2.181, 6.98, 6.101, 6.106
51(e)(3): §2.181
51(e)(5): §§2.181, 6.101
51.2: §6.101
51.2(a): §6.103
51.2(c): §6.103
51.2(d): §6.103
51.3: §§6.61, 6.103
51.3(b)(1): §6.103
51.3(b)(3): §6.103
51.3(b)(4): §6.103
51.3(c): §6.103
51.4: §6.103
51.9: §§2.152, 15.22
51.11(b)(4): §6.103
51.11(j): §6.103
51.12: §6.103
52(a): §6.101
53: §6.103
54(b): §6.103
658: §§4.32, 6.7
660: §6.8
663: §6.7
670: §11.82
671: §10.24
681: §10.25
682: §§4.21, 6.86
682-687: §10.29
682.1: §6.86
682.1(a): §§4.21, 6.91
683: §§4.22, 6.87, 10.31
683.2: §10.58
683.2(a): §10.58
684: §6.92
685: §§4.22, 10.32
685-686: §6.88
686: §10.38
687: §6.89
700: §13.16
715-719: §§8.16, 12.23
717: §1.27
718): §1.27
761: §§10.10, 10.25, 10.28
762: §10.10
801: §11.67
801(12): §4.65
802: §11.67

803: §11.43
811: §§11.58, 11.62, 11.71
811(1): §11.59
811(2): §11.60
811(3): §11.61
811(4): §11.63
813: §11.77
818: §10.52
830: §§11.82-11.83
830-831: §§11.15, 11.103
831: §11.25
840: §10.52
841: §11.36
845: §11.6
880.020-880.370: §4.52
880.020-887.090: §11.115
882.020-882.040: §4.52
884.010: §8.18
884.010-884.030: §§8.73, 8.81
885.010-885.070: §4.52
886.010-886.050: §4.52
895-945.5: §6.64
896: §6.64
900: §6.64
910-938: §6.64
910-945.5: §6.64
912: §6.64
912(b): §6.64
912(c): §6.64
912(d): §6.64
912(f): §6.64
912(g): §6.64
912(h): §6.64
912(i): §6.64
954: §12.20
1001: §§11.47, 11.87
1007: §§11.57, 11.77
1008: §§11.57, 11.77
1009: §11.77
1009(d): §11.87
1014: §§11.82, 11.110
1015: §11.86
1016: §11.84
1017: §11.84
1018: §11.84
1039: §10.1
1040: §10.13
1045: §10.1
1053: §§10.1, 10.6
1054: §§10.1, 10.71, 15.26
1055: §§10.1, 10.53
1056: §§10.72, 15.26
1057: §§10.1, 10.72, 10.76, 15.26
1057.3: §4.100
1057.3(a): §6.13
1057.3(b): §6.13
1057.3(c): §6.13
1057.6: §6.66
1058.5: §6.106B
1059: §10.74
1066: §11.49
1069: §§10.42, 11.15
1084: §§10.44, 11.1, 11.106
1086: §2.112
1086-1090: §2.39

1086(b): §§2.98, 2.105
1086(f): §2.54
1086(i): §§2.105, 2.112-2.113, 2.115
1087: §2.39
1088: §2.39
1091: §§3.25, 10.1, 10.6, 10.55, 10.60
1092: §§10.2-10.3, 10.23, 10.35
1095: §10.60
1096: §§10.15, 10.20
1098: §6.46A
1099: §§4.79, 6.59
1099(a): §6.59
1099(c): §6.59
1099(d): §6.59
1101.11: §6.35
1101.12: §6.35
1102: §8.17
1102-1102.17: §§2.153, 2.179, 4.120, 6.35, 7.36, 7.46, 10.2
1102-1103.14: §1.59
1102(a): §6.35
1102(b): §§6.35-6.36
1102(c): §§4.120, 6.35
1102.1: §6.34
1102.1(a): §§6.9, 6.35
1102.2: §§6.42, 6.57
1102.2(a): §6.35
1102.2(b): §6.35
1102.2(c): §6.35
1102.2(d): §6.35
1102.2(e): §6.35
1102.2(f): §6.35
1102.2(g): §6.35
1102.2(h): §6.35
1102.2(i): §6.35
1102.2(j): §6.35
1102.3: §§6.35-6.36
1102.3(b): §§6.35-6.36
1102.4(a): §6.35
1102.4(b): §6.35
1102.4(c): §6.35
1102.5: §6.35
1102.6: §§6.35-6.36, 7.36, 11.76, 12.22
1102.6(a): §8.17
1102.6(b): §§6.38, 8.17
1102.6(e): §6.42
1102.6a: §§4.81, 6.49
1102.6a(a): §6.38
1102.6a(c): §6.38
1102.6b: §§1.59, 4.60
1102.6b(a)(1): §6.42
1102.6b(b): §6.42
1102.6b(d): §6.42
1102.6c: §§1.59, 4.60, 6.43
1102.6d: §6.36
1102.6e: §6.46A
1102.7: §6.35
1102.8: §6.34
1102.9: §6.35
1102.10: §6.35
1102.13: §6.35
1102.15: §§1.59, 6.44
1102.16: §§1.59, 6.45
1102.17: §§1.59, 6.46
1102.18: §4.49
1103: §§4.81, 6.47, 8.17

1103-1103.4: §10.2
1103-1103.14: §1.59
1103(c): §6.48
1103(d): §6.47
1103.1: §6.47
1103.1(b): §6.48
1103.2: §§4.81, 6.49
1103.2(a): §4.81
1103.2(e): §§4.81, 6.49
1103.2(g): §6.49
1103.3(a)-(b): §6.47
1103.3(c): §6.47
1103.4(a): §6.47
1103.4(b): §6.47
1103.4(c)(1): §6.49
1103.4(c)(2): §6.49
1103.4(c)(3): §6.49
1103.5(a): §6.47
1103.5(b): §6.47
1103.7: §6.47
1103.8: §6.47
1103.10-1103.11: §6.47
1103.13: §§4.81, 6.47
1104: §§10.2, 10.44, 11.1, 11.54, 11.56, 11.106
1105: §§10.2, 10.28, 10.44
1106: §§10.2, 12.10
1107: §15.86
1108: §10.2
1109: §10.2
1110: §10.2
1111: §4.73
1112: §§10.44, 11.15-11.16, 11.25, 11.30, 11.103
1113: §§4.64, 4.111, 6.30, 10.2, 10.23, 10.37, 11.5, 12.1-12.2, 12.5-12.8, 12.12-12.13, 12.22-12.23
1113(2): §§12.7, 12.14
1114: §12.7
1115: §§12.11, 12.20
1134: §§6.60, 6.62, 10.2
1134(a): §6.62
1134(b): §6.62
1134(d): §6.62
1134(e): §6.62
1134(f): §6.62
1134(g): §6.62
1169-1172: §§11.25, 11.54
1169-1220: §15.85
1170: §15.92
1181: §15.89
1181-1182: §10.67
1181-1183.5: §15.17
1185: §§10.54, 15.89
1185(a): §15.89
1185(b)(3): §15.89
1188: §15.89
1189: §§10.65, 10.67, 15.89
1189-1190: §§10.54, 10.67
1189(b): §15.89
1195: §§10.70, 15.89
1195(a): §10.70
1195(b): §15.89
1196-1197: §15.17
1198: §10.70
1203-1204: §10.70
1206-1218: §11.54
1207: §§10.6, 10.70, 15.87, 15.89
1213: §§10.1, 12.2, 15.85, 15.87, 15.90, 15.92

1213-1215: §11.10
1213-1218: §11.25
1213-1220: §§10.2, 12.2
1214: §§8.18, 9.47, 10.2, 10.13, 12.2, 15.85-15.86
1215: §§10.1, 12.2, 15.87
1216: §10.60
1217: §§10.1, 10.6, 10.15, 15.86
1219: §10.68
1350-1359: §11.24
1350-1378: §§6.60, 6.105
1352.5: §6.102
1354(a): §10.2
1359: App O
1360(a)(2): §6.105
1362: §10.16
1365: §6.61
1365(a): §6.63
1368: §§1.59, 6.60-6.61
1368(a)(1): §6.61
1368(a)(2): §6.61
1368(a)(3): §6.61
1368(a)(4): §6.61
1368(a)(5): §6.61
1368(a)(6)-(7): §6.61
1368(a)(8): §6.61
1368(b): §6.61
1368(d)-(e): §6.61
1375: §6.61
1375.1: §6.61
1436: §6.21
1457: §4.155
1458: §12.20
1460: §12.20
1460-1468: §12.1
1462-1463: §§12.9-12.10, 12.19
1463: §§12.10, 12.19
1465: §12.20
1468: §§11.7, 12.1, 15.88
1469-1470: §12.1
1471: §§7.39, 12.1
1479: §9.45
1542: §§4.173, 7.62
1550: §§2.43, 3.16, 4.6-4.7
1550(3): §4.10
1556: §4.7
1556-1559: §2.43
1565: §§3.16, 4.8
1565-1590: §2.43
1566: §4.8
1567-1568: §4.8
1572: §6.30
1583: §8.20
1585: §6.5
1586: §6.5
1595-1599: §2.43
1596: §4.10
1598: §4.10
1599: §4.10
1605: §4.11
1605-1615: §2.43
1610: §9.107
1614: §10.13
1624: §4.13
1624(a): §§2.47, 2.64, 2.86
1624(a)(3): §§3.25, 4.6, 4.9, 4.12, 8.15, 10.1, 11.14

1624(a)(4): §§2.26-2.27, 2.43-2.45, 2.52, 2.91, 2.95, 4.135
1624(a)(6): §§4.6, 4.41, 9.48
1633.1-1633.17: §§2.47, 4.12
1633.8: §2.47
1635-1663: §6.4
1636: §6.4
1644: §6.4
1645: §6.4
1646.5: §4.158
1651: §6.4
1654: §§4.158, 4.178, 8.78
1657: §§4.83, 8.9
1662: §§4.137-4.138, 4.176, 6.4, 8.30, 13.2-13.5, 13.10-13.11, 13.13, 13.18-13.19, 15.27
1662(a): §§13.3-13.6, 13.9, 13.14
1662(b): §§4.137, 13.3, 13.8
1667: §4.10
1671: §§4.142, 4.177, 6.10
1671-1681: §§2.78, 2.119, 3.12, 3.35, 8.39
1671(b): §§4.142, 6.12
1671(d): §4.148
1675: §§2.119, 4.142, 6.13
Law Revision Commission Comments: §6.12
1675-1681: §§4.142, 6.10
1675(a): §6.10
1675(c): §§6.11, 6.14
1675(d): §§6.11, 6.14
1675(e): §6.14
1675(e)(1): §6.12
1675(e)(2): §§6.12-6.13
1675(f): §6.14
1675(f)(1)(A): §6.14
1675(f)(1)(B): §6.14
1675(f)(2): §6.14
1675(f)(3): §6.14
1675(g): §6.14
1675(g)(1)(A): §6.14
1675(g)(3): §6.14
1675(g)(9): §6.14
1675(h): §6.14
1676: §4.177
1677: §§2.119, 4.177
1677(a): §§4.142, 6.11
1677(b): §§4.142, 6.11
1678: §§2.119, 4.142, 6.11
1679: §6.10
1680: §6.11
1689: §2.148
1689(b)(7): §4.16
1692: §4.147
1695: §6.107
1695-1695.17: §6.107
1695.1(a): §6.107
1695.1(b): §6.107
1695.1(c): §6.107
1695.1(e): §6.107
1695.2: §6.108
1695.3: §6.108
1695.3(g)-(h): §6.108
1695.4(c): §6.108
1695.5(a): §6.108
1695.5(b): §6.108
1695.5(c): §6.108
1695.5(d): §6.108
1695.6: §6.109
1695.6(b): §6.109

1695.6(c): §6.109
1695.6(d): §6.109
1695.6(e): §6.109
1695.7: §6.109
1695.8: §6.109
1695.12: §6.109
1695.13: §§2.8B, 6.109
1695.14: §6.109
1698: §§4.162, 9.81
1698(b): §§2.53, 2.95
1698(c): §2.53
1709: §2.155
1710: §6.30
1710.2: §6.65
1710.2(a): §6.65
1710.2(d): §6.65
1717: §4.153
1717(a): §15.31
1750-1784: §13.123
1770(a)(22): §2.12
1916.1: §2.9
1916.5(a)(5): §9.45
1917-1917.006: §8.55
1946: §4.72
1950.5: §§4.136, 15.46
1950.7: §15.46
2020: §§2.127, 2.140
2079: §§2.153, 6.36
2079-2079.6: §2.150
2079-2079.11: §2.178
2079-2079.24: §§2.153, 6.72
2079.2: §2.142
2079.4: §2.178
2079.5: §§2.178, 6.72
2079.7: §1.59
2079.7(a): §6.54
2079.7(b): §6.54
2079.8: §1.59
2079.8(a): §6.52
2079.8(b): §6.52
2079.9: §1.59
2079.10: §§1.59, 6.70
2079.10(b): §6.70
2079.10a: §6.56
2079.10a(1): §6.56
2079.10a(a)(3): §6.56
2079.10a(b): §6.56
2079.10a(b)-(c): §6.56
2079.12: §2.150
2079.12(a)(4): §6.72
2079.13-2079.24: §§2.31-2.32, 2.35-2.36
2079.13(b): §§2.15, 2.20
2079.13(d): §§2.35, 2.129
2079.13(n): §2.31
2079.14: §§2.31, 2.37
2079.14(a): §2.31
2079.14(b): §2.31
2079.14(d): §2.31
2079.16: §§2.31, 2.146
2079.17: §§2.31, 2.37, 2.129
2079.17(a): §2.37
2079.17(a)-(b): §2.31
2079.17(b): §2.37
2079.18: §§2.33-2.34
2079.19: §2.38

2230: §2.184
2235 (former): §2.132
2295: §2.38A
2295-2357: §7.44
2295-2400: §2.27
2299: §2.28
2300: §2.30
2307: §§2.28-2.29
2308: §2.26
2310: §2.29
2315: §2.42
2319: §2.42
2332: §§2.184, 6.30, 15.20
2333: §2.184
2338: §2.184
2343(2): §2.180
2343(3): §2.179
2356: §10.60
2373-2382 (former): §2.35
2782: §14.38
2782(a): §14.38
2782(c): §14.40
2782(d): §14.40
2787-2856: §7.82
2848-2849: §4.42
2889: §10.41
2898: §9.67
2906: §8.55
2912: §9.100
2920-2944: §9.22
2920-2944.7: §2.8B
2920(b): §9.17
2923.1: §2.8B
2923.5: §§9.7, 9.55A
2923.5-2923.52: §9.55A
2923.52: §9.55A
2923.53: §9.55A
2924-2924*l*: §§9.17, 9.19, 10.41
2924a-2924*l*: §9.22
2924b: §§9.13, 9.63
2924b(c)(1): §10.9
2924b(f): §15.87
2924c: §9.47
2924e: §9.47
2924.7(b): §13.26
2925: §10.13
2929.5: §§7.90, 7.94
2930: §10.2
2941: §9.100
2943: §§4.39, 6.106E, 9.43, 15.13
2944.6: §2.8B
2944.6-2944.7: §2.8B
2944.7: §2.8B
2945.1: §2.8B
2947-2955.5: §9.22
2948.5: §15.74
2952: §10.68
2953: §10.41
2953.2: §§9.89-9.91
2953.2(b): §9.90
2953.2(c): §9.91
2953.3: §§9.89, 9.92
2953.3(b): §9.92
2953.3(c): §9.93
2953.4(c): §9.94

2953.5(a): §9.89
2953.5(b): §9.89
2954.9: §§9.30, 9.45
2954.9(a)(1)-(2): §9.31
2954.9(a)(3): §9.30
2954.9(b): §§9.31, 9.45
2954.10: §9.52
2954.11: §§9.30, 9.45, 9.52
2955.5(a): §13.26
2956: §§6.69, 9.13
2956-2957: §9.13
2956-2967: §§9.10-9.11, 15.74
2957(a): §9.10
2957(a)(1): §6.69
2958: §§6.69, 9.13
2963: §§6.69, 9.13
2963(a)-(p): §9.13
2965: §9.10
2966: §§6.69, 9.11
2966(a)(1): §6.69
2966(a)(2): §6.69
2966(a)(3): §6.69
2966(a)(4): §6.69
2985: §§4.142, 6.35, 9.15, 9.17
2985.1-2985.6: §9.17
2985.3: §9.63
2985.4: §9.17
2985.5: §9.17
2985.6: §§9.17, 9.30
2995: §2.71
3046: §9.1
3050: §10.45
3094: §4.78
3097: §4.78
3109-3154: §4.69
3115-3116: §4.69
3144: §4.69
3154: §4.69
3275: §§4.177, 9.18
3287: §4.145
3287(a): §13.113
3294: §§2.162, 13.112, 13.117, 13.117B
3294(b): §13.117B
3295(d): §§13.118B, 13.118E
3300: §§2.156-2.157, 4.140, 4.144, 4.146, 12.18, 15.22
3301: §3.29
3304: §§12.18-12.19
3304-3306: §12.1
3305: §12.18
3306: §§2.96, 4.140, 4.144-4.145, 8.33
3307: §§4.140-4.141, 4.143
3333: §§2.155, 2.157, 2.159, 15.22
3343: §§2.156, 4.147, 6.35, 8.13
3358: §4.141
3369: §4.177
3384-3395: §§4.143, 4.149
3386: §4.149
3387: §4.143
3390: §11.14
3390(5): §§4.6, 4.9
3391(2): §§4.11, 9.75
3394: §4.143
3395: §4.153
3399: §13.25
3439-3439.12 (former): §10.13

3439-3449: §10.13
3440: §11.118
3482: §6.33
3522: §10.44
5895.10-5898.32: §1.59

CODE OF CIVIL PROCEDURE
12a: §4.152
321-325: §§11.1, 11.77
322-323: §11.57
323: §11.77
323(4): §11.77
324-325: §11.57
325: §11.77
337: §§12.21, 15.22
338(b): §7.20
339: §15.22
340.9: §13.93
386-386.6: §§1.131, 15.98
386.5: §15.98
386.6: §15.98
405.20-405.24: §4.116
405.21: §10.68
409.9 (former): §4.116
446: §10.67
564: §7.94
564(c)-(e): §7.90
580a: §7.95
580a-580d: §9.22
580b: §§1.51, 4.33, 4.41-4.42, 6.106B, 7.93, 7.95, 9.1, 9.8-9.9, 9.16, 9.48, 9.55, 9.72, 9.95-9.99, 13.26
580d: §§1.51, 4.42, 7.93, 7.95
594: §2.166
638(1): App O
701.540(h): §10.9
704.910-704.950: §4.19
704.910-704.995: §§10.57, 15.89
704.930(b): §15.89
704.940: §10.57
725a-730.5: §9.22
726: §§1.51, 4.33, 7.90, 7.93, 7.95, 10.41
726(c): §10.9
726.5: §§7.90, 7.93
731a: §6.46
736: §§7.90, 7.93, 7.95
736(a): §7.95
736(b): §7.95
736(c): §7.95
751.02-751.28: §11.117
760.010-764.080: §11.112
771.010: §11.116
771.020: §11.116
871.1-871.7: §11.114
872.820: App O
1021: §4.153
1060: §11.113
1094.5: §2.173
1161: §§4.72, 9.16
1161(1): §§4.72, 4.136
1161(2): §4.74
1179: §9.18
1240.010-1273.050: §11.87
1265.225: §9.110
1275-1279.6: §10.15
1280-1294.2: §§6.15, 13.97
1282-1284.3: §13.97

1283.05: §4.177
1286-1286.6: §4.150
1287.4: §2.164
1297.71: §4.150
1297.72: §4.150
1298: §§2.85, 4.150, 6.15-6.16, 6.18-6.18A
1298-1298.8: §7.84
1298(a)-(b): §4.150
1298(b): §§4.150, 6.16
1298(c): §§4.150, 6.16
1298.7: §§6.17-6.18
1300(c): §15.25
1500-1582: §§6.35, 15.25
1530: §15.25
1560: §15.25
1775-1775.15: §4.150
1856: §4.159
1856(a)-(b): §4.159
1857: §11.15
1866: §11.15
1933: §10.54
1971: §§3.25, 4.9, 4.12, 11.14
1972: §4.13
2077: §§11.15, 11.36, 11.82-11.83, 11.90, 11.96, 11.98, 11.103, 11.110
2077(4): §11.103
2618-2622 (former): §11.77

COMMERCIAL CODE
2201: §3.26
2202: §4.159
2202(b): §4.159
2305: §3.21
6101-6111: §§4.122, 5.23, 5.25, App Q
6103(a)(1): §5.23
6103(a)(2): §5.23
6103(b): §5.23
6103(c)(12): §5.23
9302: §4.33
9401: §§4.33, 10.68
10101-10600: §5.12

CORPORATIONS CODE
207: §10.20
207(a): §4.28
208: §10.20
313: §§4.28, 10.20, 10.65
1002: §4.28
2203(c): §10.20
2258: §10.20
15501-15533: §§4.25, 10.18
15611-15724: §§4.25, 10.18, 10.64
15621: §§4.25, 4.156, 10.18, 10.64
15621(d): §4.25
15633: §4.25
15643: §10.64
15643(a): §10.64
15712(b)(1): §§4.25, 10.18
15900-15912.07: §§4.25, 10.18, 10.64
15902.01: §§4.25, 4.156, 10.18, 10.64
15902.01(e): §4.25
15903.6: §4.25
15904.03: §10.64
15904.06(b)(2): §10.64
15912.06(a)(2): §§4.25, 10.18
16100-16962: §§4.24, 10.17, 10.64

16105: §§10.17, 10.64
16111: §10.64
16201: §6.92
16202(a): §6.92
16203: §6.92
16203-16204: §10.17
16204: §§4.7, 4.24
16301: §10.64
16301-16302: §§4.24, 10.17
16301(2): §4.24
16302: §§4.7, 4.24, 10.64
16302(a)(1): §10.64
16302(b): §§4.24, 10.64
16303: §§4.24, 10.17, 10.64
16303(c): §4.24
16303(d)(2): §§4.24, 10.17, 10.64
16303(e): §4.24
16501: §§4.24, 6.92, 10.17
16502: §6.92
16601(7)(A): §6.92
16701(a): §6.92
16951-16962: §4.26
16955: §4.26
17000-17654: §4.27
17003: §4.7
17050: §§4.27, 4.156
17052(f): §4.27
17151(b)-(c): §4.27
18105: §10.16
18120: §10.16
21200: §10.16
25000-25707: §2.11
25019: §2.11
25206: §2.11
25210: §2.11

ELECTIONS CODE
9141: §4.86
9144: §4.86
9235: §4.86
9237: §4.86

EVIDENCE CODE
250: §1.9
622: §§4.73, 10.38
623: §3.26
641: §4.151
642: §10.45
662: §§10.2, 11.11
1451: §10.69

FAMILY CODE
297: §6.96
297(a): §6.90
297(b): §6.90
297.5: §§6.86, 6.90
297.5(a): §6.90
297.5(c): §6.90
308: §6.89
308.5: §6.89
700: §§10.26, 10.29, 10.38
721: §10.39
750: §§4.21, 6.89
751: §6.89
752-754: §10.57

760: §§4.21, 6.89, 10.26, 10.29, 10.33, 10.38
770: §§4.21, 10.29
803: §§10.26, 10.29, 10.38-10.39
850-853: §6.89
1102-1103: §10.57
1102(a): §4.19
1500: §6.89
2550: §6.89
2580-2581: §§4.21, 10.33
2581(a): §4.21
2640: §10.33
6321: §10.57
6500: §4.15
6701: §10.76
6701(b): §4.15
7002: §4.15
7050(e)(3): §4.15
7122: §4.15

FINANCIAL CODE
1227: §9.67
1227.3: §13.26
1560: §9.67
4995-4995.6: §2.8B
17000-17703: §§2.22, 15.3-15.4
17003(a): §15.1
17004: §15.2
17004.5: §15.5
17005.6: §15.5
17006: §15.6
17006(a): §15.6
17006(a)(2): §2.23
17006(a)(4): §2.22
17006(b): §§2.22, 15.6
17200: §§2.22, 15.6
17203.1: §15.4
17300-17350: §15.4
17310-17315: §15.27
17312(c): §15.4
17403.5: §15.5
17404: §15.4
17406: §15.4
17409: §15.4
17409.1: §15.4
17415: §15.4
17421.5: §15.97
17607: §15.4
17608: §15.4
17621: §15.4
17635: §15.4
17700: §15.4
17701: §15.4
22100: §2.7
22161(a): §2.8B

FISH AND GAME CODE
2050-2116: §7.1

GOVERNMENT CODE
16: §10.59
16.5: §2.47
8589.3: §6.48, App N
8589.3-8589.4: §4.81
8589.3-8589.5: §1.59
8589.4: §6.48, App N

8589.5: §6.48
8875.6-8875.95: §1.59
8893.2: §4.81
8893.3(j): §6.52
8897.1-8897.2: §1.59
8897.1(a): §6.52
8897.1(c): §6.52
8897.2(a): §6.52
8897.2(b): §6.52
9605: §2.8B
11500-11529: §2.173
11502: §2.173
11503: §2.173
11507.5-11507.7: §2.173
11511: §2.173
11513: §2.173
11517: §2.173
11517(c): §2.173
11521(a): §2.173
11522: §2.173
11523: §2.173
12651(a)(1)-(2): §14.66
12651(a)(8): §14.66
12900-12996: §§2.181, 6.98, 6.102
12920: §2.181
12921(b): §2.181
12927(c)(1): §6.102
12927(c)(2): §6.102
12948: §2.181
12955: §6.102
12955(a): §2.181
12955(d): §2.181
12955(j): §2.181
12955(m): §6.102
12955.2: §6.103
12955.4: §6.102
12955.6: §6.103
12955.9: §§6.102-6.103
12955.9(a): §6.103
12955.9(b)(1): §6.103
12955.9(b)(2): §6.103
12955.9(b)(3): §6.103
12956.1(c): §6.102
12956.2: §6.102
12980-12989.3: §6.102
12980(a): §6.102
12993(c): §6.102
23071-23076: §11.15
23073-23076: §11.103
24250: §15.90
27201: §12.2
27201-27399: §15.85
27203-27203.5: §15.87
27248: §12.2
27257: §12.2
27279.1: §15.88
27279.3: §15.88
27282(a)(1): §10.68
27282(a)(3): §10.68
27282(a)(4): §10.68
27282(a)(5): §10.68
27283-27285: §10.68
27285-27286: §10.68
27287: §§10.46, 15.89
27287-27288: §10.67

27288: §§8.81, 15.89
27288-27290: §12.2
27288.1: §15.88
27293: §15.88
27320: §10.8
27321: §10.9
27321.5: §§10.10, 15.88
27322: §10.60
27330: §10.68
27361: §15.91
27361.6: §§10.8, 15.88
27361.7: §10.36
38780: §6.40
38781: §6.40
38783: §6.40
38784: §6.40
38785: §6.40
51100-51119.5): §1.80
51178: §6.48, App N
51179: App N
51182: §6.48, App N
51183.5: §§1.59, 4.81, 6.48
51200-51297.4: §§1.86, 4.93
51252: §4.93
53311-53368.3: §§1.59, 4.60, 4.171, 6.42
53340.2: §§4.60, 6.42
53754: §§4.60, 6.42
56000-57550: §4.91
56000-57550): §1.86
56301: §4.91
56375: §4.91
56375(a): §4.91
56650: §4.91
56700-56711: §4.91
56750-56762: §4.91
56755(a): §4.91
65300-65403: §1.75
65302: §1.75
65303: §1.75
65450-65457: §1.76
65700: §1.75
65800-65917.5.65918: §1.77
65853: §4.86
65854-65855: §4.86
65855-65856: §4.86
65860(c): §4.86
65864-65867.565869.5: §1.84
65864-65869.5: §4.86
65865.4: §1.84
65901: §4.87
65906: §4.87
66410-66499.37: §§4.31, 4.92, 4.114, 9.100, 9.103, 9.106, 10.76, 11.24, 11.87A
66410-66499.37): §1.83
66411: §1.83
66411-66411.1: §§4.92, 9.103
66412: §4.92
66418-66419: §4.92
66424: §§1.83, 4.92, 9.103
66426: §9.103
66428: §9.103
66433-66463.5: §9.103
66451-66472.1: §1.83
66451.10-66451.32: §11.87A
66451.11: §§10.13, 11.87A
66451.11(a): §11.87A

66451.11(b): §11.87A
66451.30: §11.87A
66466: §11.100
66473: §1.79
66473.5: §§1.76, 1.79
66474: §1.76
66474.2: §1.84
66474.4: §4.93
66474.4(f): §4.93
66495-66496: §11.12
66498.1-66498.9: §1.84
66498.1(b): §1.84
66499.30: §4.92
66499.30(a)-(b): §4.92
66499.30(e): §§4.92, 11.24
66499.32: §§4.92, 11.24
66499.34: §§1.79, 4.92
66499.35(a): §4.92
66499.35(c): §§4.92, 4.114
66499.35(d): §4.92
66499.50-66499.58: §§11.24, 11.93
66500-6653266537: §1.86
66600-6667066694: §1.86
66620: §6.49
66800-66801: §1.86
67000-67130: §1.86

HEALTH AND SAFETY CODE
Div 20: §1.82
1366.20-1366.29: §§5.18-5.19, App Q
1500-1567.8: §6.33
1566.5: §6.33
1569.2(k): §6.104
1569.87: §6.104
1596.78: §6.104
1597.40: §6.104
5411.5: §7.53
8550-8557: §11.24
13113.7-13113.8: §6.57
13113.8: §1.59
13113.8(b): §6.57
13113.8(c): §6.57
13113.8(d): §6.57
13113.8(g): §6.57
13113.8(h): §6.57
13113.9: §1.59
17958.4: §6.45
18007: §6.35
18008: §6.35
19211(a): §6.58
19211(b): §6.58
19211(d): §6.58
25100-25250.28: §7.48
25100-25250.2725257.1: §1.82
25100-25257.1: §§7.9, 7.76
25101(d): §7.9
25117: §§4.173, 7.9
25140-25141: §7.9
25160: §7.76
25189: §7.53
25229: §7.41
25232(a)-(b): §7.41
25249.5: §4.173
25280-25299.206: §§7.6, 7.8
25281(h): §7.9

25300-25395.15: §12.1
25300-25395.32: §1.82
25300-25395.45: §§7.9, 7.17, 7.22, 7.48, 7.61
25316: §§4.173, 7.9
25317: §7.9
25323.5: §7.11
25323.5(b): §7.22
25358.3(a)(1): §7.15
25358.3(a)(3): §7.15
25359(a): §7.15
25359.2: §7.15
25359.4: §7.53
25359.4.5: §7.15
25359.7: §§1.59, 1.64, 4.49, 4.80, 4.120, 7.61
25359.7(a): §§1.64, 7.36, 7.40, 7.46, 7.53
25359.7(b): §7.36
25360: §7.16
25363(e): §§7.16-7.17, 7.67
25364: §§7.21, 7.58, 7.61
25375(a)(3)(A): §7.18
25395.60-25395.109: §7.32
25395.60-25395.119: §7.22
25395.66: §7.35
25395.69: §§7.22, 7.32
25395.69(a): §7.34
25395.70: §7.22
25395.79.2(a): §7.33
25395.79.2(b): §7.33
25395.79.2(c)(1): §7.33
25395.79.2(c)(2): §7.33
25395.80: §§7.32, 7.34
25395.81: §7.35
25395.81(a)(1): §7.35
25395.83: §7.35
25395.84: §7.35
25395.85: §7.35
25395.86(a)(1): §7.35
25395.86(a)(2): §7.35
25395.86(a)(3)-(4): §7.35
25395.86(b): §7.35
25395.86(c): §7.35
25395.116: §7.32
25395.116(c)(1): §7.32
25395.116(c)(3): §7.32
25395.116(d): §7.32
25400.10-25400.47: §6.55
25400.22: §6.55
25400.28(a): §6.55
25401-25402.3: §7.15
25548-25548.7: §7.88
25548(b): §7.88
26100-26156: §§4.49, 4.82
26100-26157: §§6.53, 13.130
26103: §4.82
26105: §4.82
26130: §4.82
26140: §4.49
26140-26147: §4.82
26140(a): §4.82
26140(d): §6.53
26143: §4.82
26145: §4.82
26150(a): §4.82
26156: §4.82
29395.64: §7.34

29395.92(a): §7.34
29395.93(b): §7.34
29395.96(a): §7.34
33459-33459.8: §7.15
39000-44474: §1.82
40000-4108241357: §1.82
40522.5: §7.7
40716: §7.7
40717(e): §7.7

INSURANCE CODE
22: §§13.73, 13.81
23: §14.32
151: §14.33
250: §§13.73, 13.81-13.82
280: §13.16
281: §13.16
282: §13.16
283: §13.16
284: §13.23
286: §§13.11, 13.22
300: §§13.8, 13.24
304: §13.24
305: §13.24
384: §14.41
384(a): §14.41
410: §13.101
411: §13.101
412: §13.101
520: §13.24
530: §§13.83, 13.86
552: §13.89
553: §13.89
677.2: §§14.32, 14.37
790-790.15: §13.93
790.03: §§13.122-13.123
790.03(h): §§13.122-13.123
790.035: §13.1118C
1861.03(a): §13.123
2051(b): §13.102
2051.5: §13.103
2051.5(a): §13.103
2051.5(c): §13.103
2058: §13.101
2070: §§13.24, 13.107
2070-2071: §13.107
2071: §§13.24, 13.30, 13.34, 13.87-13.89, 13.91, 13.93, 13.96, 13.107
2071(a): §§13.88, 13.90, 13.92-13.93, 13.96-13.97
2071.1: §13.92
2071.1(a)(1): §13.92
2071.1(a)(2): §13.92
2071.1(a)(3): §13.92
2071.1(a)(4): §13.92
2071.1(a)(5): §13.92
2071.1(a)(6): §13.92
2079: §§13.93, 13.107
10089.5-10089.54: §13.52
10101: §§13.107, 13.109
10101-10107: §13.107
10102: §§13.103-13.104, 13.107, 13.109
10102(a): §13.104
10102(e): §13.109
10103(a)(2): §13.109
10103(a)(5): §13.109
10103.5(a): §13.98

10103.5(b): §13.98
10103.5(c)(2): §13.98
12340-12417: §15.15
12340.2: §11.10
12340.6: §15.3
12340.10: §11.13
12340.11: §§4.55, 6.80, 11.10
12404-12413.5: §2.5
12413.1: §§4.35, 15.35
12414.30(b): §6.80

LABOR CODE
1400-1408: §5.19, App Q
1401: §5.18
2802: §2.20
2802(a): §2.20
2804: §2.20
3200-6208: §2.18
3350-3351: §2.18
3353: §2.18

MILITARY AND VETERANS CODE
985-989.9: §9.54
987: §9.45
987.1: §9.54
987.16: §9.54

PENAL CODE
290.4: §6.56
290.45: §6.56
290.46: §6.56
2600: §4.18
2600-2601: §10.24
2601(a): §4.18

PROBATE CODE
100-101: §6.89
223: §10.31
630-631: §10.52
1400-3803: §4.17
2109: §10.22
2111: §10.22
2420(b): §4.17
4000-4805: §10.60
6101: §6.89
6401: §6.89
7263: §§10.19, 10.63
9734: §8.27
10161-10168: §1.106
16000-16015: §2.124
16002: §2.132
16004: §2.132
16463: §2.132
18100: §10.47
18100.5: §6.80
18101: §10.47
21205: §8.16
21225: §8.16

PUBLIC RESOURCES CODE
2621-2630: §6.48
2621-2630): §1.86
2621.9: §§1.59, 4.81, 6.48
2622: App N
2690-2699.6): §1.86

2694: §§1.59, 4.81, 6.48
2696: §6.48, App N
4125: §6.48, App N
4136: §§1.59, 4.81, 6.48
4142: App N
4291: App N
4511-4517) and: §1.80
6210.8: §11.85
6357-6360: §11.82
6461: §11.85
8801-8819: §11.22
8801(a): §11.22
8801(b): §11.23
8801(e): §11.23
8803-8809: §11.22
8814: §11.22
21000-21001: §4.94
21000-21177: §§1.82, 4.94, 7.1
21002: §4.94
21002.1(e): §4.97
21060.5: §4.95
21064.5: §4.96
21065: §4.95
21068: §4.95
21080: §§4.86, 4.95
21080(b): §4.96
21080(e)(1): §4.95
21080.01-21080.33: §4.96
21100: §4.95
21100): §1.82
21108: §4.98
21151: §4.95
21151.5(a): §4.95
21167: §4.98
21167.1: §4.98
25401.7: §6.77
25402.9: §6.70
25402.10(d): §4.49
25402.10): §1.59
25942: §6.70
30000-30900: §4.88
30000-30900): §1.86
30103: §4.88

PUBLIC UTILITIES CODE
2871-2876: §2.12
7901: §11.50

REVENUE AND TAXATION CODE
50: §§1.96, 6.96
60: App A
61(a): App A
61(b): App A
61(c): App A
61(e): App A
61(f): App A
61(g): App A
61(h): App A
61(i): App A
61(j): App A
62: §§6.86, 6.90, App A
62(a): §6.96, App A
62(a)(2): §1.96, App A
62(b): App A
62(c)(1): App A

62(c)(2): App A
62(d): §6.96, App A
62(d)(1): App A
62(d)(2): App A
62(e): App A
62(f): App A
62(g): App A
62(i): App A
62(*l*): App A
62(m): App A
62(n): App A
62(o): App A
62(p): §6.96
62.1-62.2: App A
63: §§6.96, 10.34, App A
63(a): App A
63(b): App A
63(c): §6.96, App A
63.1: App A
63.1(a): §6.96
63.1(a)(1): App A
63.1(a)(2): App A
63.1(a)(3): §6.96, App A
63.1(b)(2): App A
64: App A
64(a): App A
64(b): App A
64(c): App A
65: App A
65(a): App A
65(b): App A
65(c): App A
65(d): App A
65(e): App A
65(f): App A
65.1: App A
67: App A
69: §6.96
69.5(a): §6.96
69.5(a)(1)-(2): §6.96
69.5(b)(7): §6.96
69.5(f): §6.96
69.5(g)(2): §6.96
69.5(g)(5): §6.96
69.5(g)(12): §6.96
74.3: §6.96
74.5: §6.96
201: §4.61
327: §11.24
401: §4.61
421-430.5: §4.93
480: §10.9
480.3: §15.99
480.3(b): §15.99
480.4: §15.99
531: §15.44
531.2: §§4.133, 15.44
2188.2: §4.61
2189: §4.61
2192: §4.60
2192.1: §§4.60, 4.63
2610.5: §4.133
2617-2618: §4.60
2821: §§4.60, 4.133
3351: §4.60

3436: §4.60
3691: §§4.60, 4.63
3693: §4.60
3771: §6.35
11901-11934: §10.11
11911: §10.11
11911-11913: §6.95
11911(a): §6.95
11911(b): §10.11
11911(b)-(c): §6.95
11912: §§6.95, 15.69
11921: §6.95
11921-11930: §§10.11, 15.91
11923: §6.95
11925: §6.95
11926: §6.95
11927: §6.95
11930: §6.95
11931: §10.11
11932: §§10.11-10.12, App G
11933: §10.11
17144.5: §6.106F
17941-17943: §4.20
18649: §9.23
18662: §§1.85, 4.132, 15.75
18662(e): §15.75
18662(e)(1): §§15.75, 15.77
18662(e)(2): §15.75
18662(e)(2)(A): §6.94
18662(e)(3): §15.76
18662(e)(3)(D): §15.79
18662(e)(3)(D)(i)(II): §15.76
18662(e)(3)(E): §15.79
18668: §15.31
18668(d): §15.79
18668(e)(1): §15.79
18668(e)(5): §15.79
18815: §4.175
19135: §1.89
23802(b)(1): §4.20
26131: §9.23

STREETS AND HIGHWAYS CODE
3114-3115: §4.63
8300-8363: §11.80
8500-8887: §§1.59, 4.60, 4.171, 6.42

UNEMPLOYMENT INSURANCE CODE
601: §2.17
650: §2.17
13004.1: §2.19

WATER CODE
13000-14076: §1.82
13260: §7.53
13264: §7.53
13271: §7.53

ACTS BY POPULAR NAME
Administrative Procedures Act: §2.173
Air Resources Law: §1.82
Alcoholic Beverage Control Act: §5.22
Alquist-Priolo Earthquake Fault Zoning Act: §§1.86, 6.48
Beverly-Killea Limited Liability Company Act: §4.27
California Coastal Act: §4.88

California Environmental Quality Act (CEQA): §§1.82, 4.86, 4.94-4.96, 4.98, 7.1
California Fair Employment and Housing Act (FEHA): §2.181
Carpenter-Presley-Tanner Hazardous Substance Account Act (HSA): §§1.82, 7.9, 7.11, 7.17, 7.22, 7.48, 7.61, 7.67, 12.1
Cartwright Act: §§2.41, 2.118
Clean Air Act: §§7.7
Coastal Act: §1.86
Community Care Facilities Act: §6.33
Consumer Legal Remedies Act: §13.123
Continuation Benefits Replacement Act: §5.18
Corporate Securities Law of 1968: §2.11
Cortese-Knox-Hertzberg Local Government Reorganization Act of 2000: §§1.86, 4.91
Davis-Stirling Common Interest Development Act (Davis-Stirling Act): §§6.60, 6.105
Development Agreements Law: §4.86
Documentary Transfer Tax Act: §§6.95, 10.11
Domestic Partner Rights and Responsibilities Act of 2003: §6.90
Drywall Safety Act of 2009: §13.137
Endangered Species Acts: §7.1
Escrow Law: §§2.22-2.23, 15.3-15.4, 15.6
Fair Employment and Housing Act (FEHA): §§2.181, 6.98, 6.102-6.103
False Claims Act (FCA): §14.66
Hart-Scott-Rodino Act: §5.25
Hazardous Waste Control Law (HCL): §§1.82, 7.9, 7.35, 7.48, 7.76
Home Equity Sales Contracts Act: §6.107
Improvement Bond Act of 1915: §§1.59, 4.60, 6.42
Land Conservation Act of 1965 (Williamson Act): §4.93
Land Reuse and Revitalization Act of 2004: §§7.22, 7.32, 7.34-7.35
Local Agency Formation Commission (LAFCO): §1.86
Map Act: §4.114
McEnerney Act: §11.117
Megan's Law: §6.56
Mello-Roos Community Facilities Act of 1982: §§1.59, 4.60, 6.42, 8.17
Methamphetamine Contaminated Property Cleanup Act of 2005: §6.55
Metropolitan Transportation Commission Act: §1.86
Polanco Redevelopment Act: §§7.15, 7.35
Porter-Cologne Water Quality Control Act: §1.82
Power of Attorney Law: §10.60
Proposition 13: §6.96
Real Estate Law: §§2.1-2.2, 2.4-2.6, 2.8A, 2.10, 2.14, 2.16, 2.20, 2.42, 2.149, 2.164-2.165, 2.167, 2.171-2.174, 2.176, 2.178, 2.181
Real Property Loan Law: §§2.7-2.8, 2.8B
Recording Act: §§10.1, 12.2
Registered Domestic Partner Rights and Responsibilities Act of 2003: §6.91
Revised Limited Partnership Act (Revised Act): §§4.25, 10.18, 10.64
Safe Drinking Water and Toxic Enforcement Act of 1986: §4.173
San Francisco Bay Conservation and Development Commission (BCDC): §1.86
Seismic Hazards Mapping Act: §1.86
Statute of Frauds: §§2.27, 2.43-2.45, 2.47-2.48, 2.50-2.52, 2.64, 2.95, 2.115, 2.119, 2.121, 2.125, 3.25-3.26, 3.44, 4.9, 4.13, 4.159, 10.1
Subdivided Lands Act: §§9.104, 15.4
Subdivision Map Act: §§1.79, 1.81, 1.83, 4.31, 4.55, 4.92, 4.114, 4.173, 9.100, 9.103, 9.106, 10.13, 11.24, 11.87A
The Vacation Ownership and Time-Share Act of 2004: §5.7
Toxic Mold Protection Act of 2001: §§4.49, 4.82, 6.53, 13.130
Unclaimed Property Law: §§6.35, 15.25
Unfair Competition Law (UCL): §13.122
Unfair Insurance Practices Act: §§13.93, 13.122-13.123
Unfair Practices Act: §13.98
Uniform Electronic Transactions Act: §§2.47, 4.12
Uniform Fraudulent Conveyance Act (former): §10.13
Uniform Fraudulent Transfer Act (UFTA): §10.13
Uniform Limited Partnership Act (ULPA): §§4.25, 10.18
Uniform Limited Partnership Act of 2008 (2008 ULPA): §§4.25, 10.18, 10.64
Uniform Partnership Act of 1994 (UPA): §§4.24, 10.17, 10.64
Uniform Vendor and Purchaser Risk Act: §§4.137-4.138, 4.176, 8.30, 13.3-13.4, 13.10, 13.18, 15.27
Unruh Civil Rights Act: §§2.181, 6.98, 6.100-6.103, 6.106
Williamson Act: §§1.86, 4.93

Workers' Compensation Act: §2.18
Z'berg-Nejedly Forest Practice Act of 1973: §1.80

SESSION LAWS
Stats 2004, ch 705: §7.35
Stats 2003, ch 421: §6.90
Stats 1996, ch 338, §1: §6.77
Stats 1986, ch 820, §7: §2.132
Stats 1986, ch 498, §1(b): §6.65

SENATE BILLS
1055: §6.106F
739: §13.137
94: §2.8B

ASSEMBLY BILLS
389: §7.22

Regulations

CALIFORNIA CODE OF REGULATIONS

Title 2
22000-22005: §2.47

Title 4
57: §5.22

Title 10
1700-1769: §15.4
2695.1-2695.14: §§13.93, 13.98
2695.4(a): §13.93
2695.7(f): §13.93
2700-3109: §2.149
2705-3109: §2.1
2725: §§2.14, 2.181
2725(e): §2.12
2726: §2.21
2740: §2.4
2752: §2.21
2755: §2.4
2770: §2.12
2770.1: §2.12
2780-2781: §2.181
2790-2804: §11.24
2791.9: §9.17
2799.1: §2.12
2830.1-2836: §§2.42, 2.67, 2.149
2832: §§2.70, 2.149
2840: §2.8
2840-2849.01: §2.7
2844: §2.8A
2844(b)(1)(A): §2.8A
2844(b)(2)(A): §2.8A
2844(b)(2)(B): §2.8A
2844(b)(2)(E): §2.8A
2844(b)(3)(A): §2.8A
2844(b)(3)(B): §2.8A
2845: §2.12A
2848: §2.12
2904: §2.135
2905: §4.79
2950: §2.22
2950-2951: §2.67
2951: §2.22

Title 14: §4.98
Div 6, Chap 3, App G: §4.95
13001-13666.4: §1.86
13170: §4.88
15000-15387: §1.82
15060-15065: §4.96
15070-15075: §4.96
15075: §4.98
15260-15285: §4.96
15268: §4.95
15300-15333: §4.96
15300.1: §4.95

Title 16
465: §11.24

Title 18
462.001: App A
462.020: App A
462.020(a): App A
462.020(b): App A
462.020(b)(1): App A
462.020(b)(2): App A
462.020(b)(2)-(3): App A
462.040(a): App A
462.040(b): App A
462.040(b)(1): App A
462.040(b)(2): App A
462.040(b)(3): App A
462.040(b)(4): §4.22
462.040(b)(4)(B): App A
462.040(b)(5): App A
462.040(b)(6): App A
462.060(a): App A
462.080: App A
462.080(b)(2): App A
462.100(a)(1)(A): App A
462.100(a)(1)(B): App A
462.100(a)(1)(C): App A
462.100(a)(2)(A): App A
462.100(b)(1)(B): App A
462.100(b)(2)(A): App A
462.100(d): App A
462.120(a)-(b): App A
462.140: App A
462.160(a): App A
462.160(b)(1): App A
462.160(b)(2): App A
462.160(b)(3): App A
462.160(c): App A
462.160(c)-(d): App A
462.160(d)(2): App A
462.160(d)(3): App A
462.160(d)(4): App A
462.180(a): App A
462.180(b): App A
462.180(b)(2): App A
462.180(c): App A
462.180(d): App A
462.180(e)(1): App A
462.180(e)(2): App A
462.220: App A
462.220(a): App A
462.220(b): App A
462.220(c): App A

462.220(e): App A
462.240(a): App A
462.240(a)(1): App A
462.240(a)(2): App A
462.240(b): App A
468-469: App A

Title 24
Prt 11 (Green Building Standards Code): §1.78

Rules

CALIFORNIA RULES OF PROFESSIONAL CONDUCT
1-100(D)(1): §1.4
1-100(D)(2): §1.4
2-100: §1.117
3-110: §1.5
3-110(A): §1.5
3-110(B): §1.5
3-300: §§1.7, 1.21
3-310: §§1.8, 1.10, 1.21
3-310(A)(1): §1.9
3-310(A)(2): §1.10
3-310(A)(3): §1.9
3-310(B): §1.9
3-310(C): §1.10
3-310(C)(1): §1.11
3-310(C)(2): §1.11
3-310(D): §1.10
3-310(E): §§1.10-1.11
3-310(F): §1.10
3-410: §1.12A
4-100: §1.12
4-200: §§1.19-1.21
4-300(A): §1.7
4-300(B): §1.7

CALIFORNIA JURY INSTRUCTIONS, CIVIL (CACI) APPROVED
1924: §2.157
2331: §13.120
2332: §13.120
2350: §13.115
3943: §13.117B

CALIFORNIA JURY INSTRUCTIONS, CIVIL (BAJI)
14.72.2: §13.1118C

Municipal Codes

BERKELEY MUNICIPAL CODE
Ch 19.16: §6.41
Ch 19.16.070: §6.41
7.52.040: §6.95

OAKLAND MUNICIPAL CODE
4.20.020: §§4.134, 6.95

SAN FRANCISCO HEALTH AND SAFETY CODE
Art 21, §1153: §6.53

UNITED STATES

Constitution

Art III: §13.122

Statutes

UNITED STATES CODE

Title 7
3501-3508: §1.89

Title 9
1-16: §§2.85, 2.154, 6.15, 6.18-6.18A

Title 11
362: §9.47
362(a): §8.28
365(a): §8.28
365(g): §8.28
523(a)(11): §2.170
1146(a): §4.134

Title 12
371(a): §9.67
1464(c)(1)(B): §9.67
1701-1750g: §9.54
1701j-3: §§4.43, 9.16, 9.50-9.52
1701j-3(b)(1): §4.43
1701j-3(b)(1)-(2): §9.50
1701j-3(d): §9.51
1709(g): §9.54
1709(r): §9.54
2601: §§6.69, 15.95
2601-2617: §§2.5, 2.8, 2.8B, 2.71, 2.135, 4.57, 6.23, 15.74, 15.95
2601(b)(1): §15.95
2601(b)(3): §15.95
2602: §2.5
2602(1): §6.23
2602(1)(A): §15.95
2603: §§6.23, 15.95
2604: §15.95
2606(a)(1): §15.95
2607: §2.5
2607(a)-(b): §2.135
2607(b)(2): §15.95
2607(c): §2.5
2607(d): §2.135
2608: §§2.71, 4.57, 15.95
2610: §15.95
5101-5116: §2.7

Title 15
1-7: §§2.41, 2.118
1(e): §2.41
18a: §§1.67, 5.12, 5.25, App Q
77a-77aa: §§2.11, 5.7
1601-1693r: §§2.8, 2.8B, 15.74
1604: §§6.69, 9.13
1639: §2.8B
6801: §15.31
7001-7031: §§2.47, 4.12
7002: §2.47

Title 16
1451-1466: §1.90
1531-1544: §7.1

Title 18
1956(c)(7): §4.173

Title 22
3101-3108: §1.89

Title 29
141-187: §5.18
621-634: §5.18
1161-1169: §§5.18-5.19, App Q
2101-2109: §5.18
2101-2109): §5.12

Title 31
5311-5330: §2.182
5312(a)(2)(U): §2.182
5318(h): §2.182
5318(h)(1): §2.182
5321(a)(1): §2.182
5321(a)(6): §2.182
5322(a): §2.182

Title 33
1251-1387: §1.90
1317(a): §7.8

Title 38
3701-3714: §9.54
3713: §9.54
3714(f): §9.54

Title 42
1981: §§6.98-6.99
1981-1982: §2.181
1981a: §§6.98-6.99
1982: §6.99
1983: §§6.98-6.99
1988: §§6.98-6.99
1988(b): §6.99
3601-3631: §§2.181, 6.98, 6.100
3602(h): §6.100
3602(k): §6.103
3603(b)(1): §§2.181, 6.100
3603(b)(2): §6.100
3604: §6.100
3604-3605: §2.181
3604(f): §6.100
3607(a): §§2.181, 6.100
3607(b)(1): §§2.181, 6.100
3607(b)(1)-(3): §§2.181, 6.100
3607(b)(2): §6.103
3610: §6.100
3610(a)-(b): §6.100
3610(f): §6.100
3610(g)(3): §6.100
3610(h): §6.100
3612: §6.100
3612(a): §6.100
3612(g): §6.100
3612(i): §6.100
3612(p): §6.100
3613: §6.100
3613(a)(2)-(3): §6.100
3613(d): §6.100
3613(e): §6.100
3614: §6.100
3615: §6.100
4001-4129: §§1.90, 13.53, 13.130

4071(a): §13.53
4072: §13.53
4321-4370f: §1.90
4851-4856: §6.51
4852d(a)(1): §6.51
4852d(a)(2)-(3): §6.51
4852d(b): §6.51
4852d(c): §6.51
4901-4918: §1.90
5154a(a): §6.68
5154a(b)(1): §6.68
5154a(b)(2): §6.68
5320: §1.90
6901: App Q
6901-6992k: §§7.8-7.9, 7.15, 7.48, 7.76
6901-6992k): §1.88
6901 et seq: §4.173
6903: §7.5
6903(5): §7.8
6921: §§7.8-7.9
6921(a): §7.8
6921(b): §7.8
6922(a)(5): §7.76
6924(a)(1)-(2): §7.76
6924(a)(7): §7.76
6926: §7.9
6972: §7.19
6972(a): §7.15
6972(a)(1)(B): §§7.8, 7.19
6972(e): §7.19
6991-6991m: §§7.6, 7.8
6991(2): §§7.8-7.9
7401-7671q: §1.90
7641-7642: §1.90
9601: App Q
9601-9675: §§4.80, 7.5, 7.8, 7.12, 7.48, 12.1
9601-9675): §1.88
9601(14): §7.8
9601(20)(A): §7.88
9601(20)(E): §7.88
9601(20)(F): §7.88
9601(22): §7.1
9601(23)-(24): §7.1
9601(25): §7.1
9601(29): §7.5
9601(35): §§7.22, 7.24-7.25
9601(35)(A): §§7.23-7.25
9601(35)(A)(iii): §7.22
9601(35)(B): §§7.24-7.25, 7.28
9601(35)(B)(iv)(I): §7.26
9601(35)(B)(iv)(II): §7.27
9601(40): §§7.30-7.31, 7.34
9601 et seq: §4.173
9602: §7.9
9602(a): §7.8
9603: §7.43
9605: §§7.16, 7.93
9606: §7.15
9606(a): §7.15
9606(b)(1): §7.15
9606(b)(2): §7.18
9606(c): §7.15
9607: §§7.14, 7.17-7.18, 7.61
9607(a): §§7.11, 7.18
9607(a)(1): §§7.11-7.12

9607(a)(1)-(2): §7.12
9607(a)(2): §§7.12, 7.16
9607(a)(3): §7.76
9607(a)(4)(A): §7.19
9607(a)(4)(A)-(B): §7.16
9607(a)(4)(B): §§7.16-7.19, 7.21, 7.67
9607(b)(1)-(2): §7.22
9607(b)(3): §§7.22-7.23, 7.25
9607(c): §7.66
9607(c)(3): §7.15
9607(e): §§7.21, 7.58, 7.61
9607(e)(1): §7.61
9607(q): §7.30
9607(q)(1)(C): §7.30
9607(q)(1)(D): §7.31
9607(q)(3): §7.30
9613: §§7.15, 7.17
9613(f): §§7.17-7.18
9613(f)(1): §7.17
9613(f)(3)(B): §7.17
9658(a): §7.20
9658(b)(4)(A): §7.20
12101-12213: App Q
14071-14073: §6.56

Title 43
772: §11.93
932 (former): §11.77

Title 47
227: §2.12

Title 49
5101: App Q

Title 50
App §2170: §1.89

INTERNAL REVENUE CODE
Subchapter C: §4.20
Subchapter S: §4.20
1(a)-(e): §9.32
108(a)(1)(E): §6.106F
108(h): §6.106F
108(h)(2): §6.106F
121: §§6.106F, 15.76
121(4): §6.97
121(a): §6.97
121(b)(1): §6.97
121(b)(2)(A): §6.97
121(b)(2)(B): §6.97
121(b)(3): §6.97
121(b)(4): §6.97
162: §9.21
162): §1.20
212(1)-(2): §1.20
212(3): §1.20
368: App A
453: §§2.66, 8.35, 9.24
453(b)(1): §9.25
453(b)(2)(A): §9.24
453(d)(1): §9.24
453(d)(2): §9.24
453(d)(3): §9.24
453(g)(1)(B)(ii): §9.38

453(i): §9.27
453(l)(1)(B): §9.32
453A(d): §9.33
453B(a)(1): §9.33
483: §§9.34, 9.36
483(c)(1): §9.36
483(d)(1): §9.36
483(d)(2): §9.36
483(e): §9.36
676: §6.97
861: §15.80
882: §15.80
897: §§1.89, 4.132, 9.23, 15.80
1014(b)(6): §10.34
1014(b)(9): §10.34
1031: §§1.96, 1.101, 4.127, 4.165, 4.178, 8.52, 9.109, 15.76
1031(a): §1.101
1031(a)(3): §1.101
1031(d): §1.101
1033: §15.76
1060: §§4.36, 4.170, 4.182
1060(a)(2): §4.36
1221: §§4.36, 6.97
1221(1): §9.32
1231: §1.54
1234(a)(1): §8.37
1234(a)(2): §8.36
1245: §9.27
1250: §9.27
1271-1275: §9.34
1272(a)(2)(C): §§9.35-9.36
1273(a)(1): §9.35
1274: §9.36
1274(b): §9.35
1274(c)(1): §9.35
1274(c)(2)-(3): §9.35
1274(c)(3): §§9.35-9.36
1274(c)(4): §9.36
1274A(a)-(b): §9.37
1445: §§1.89, 4.132, 4.175, 9.23, 15.80
1445(a): §§6.94, 9.23
1445(b)(2): §15.81
1445(b)(4)(B): §9.23
1445(b)(5): §15.81
1445(b)(7): §15.84
1445(b)(9): §15.81
1445(c): §15.83
2035: §10.13
2512(b): §10.13
3102(a): §2.19
3401-3403: §2.19
3501-3510: §2.19
3508(b): §2.19
6038A: §1.89
6038C: §1.89
6039C: §15.80
6045(e): §4.175
6166: §4.62
6321: §4.62
6323: §4.62
6324: §4.62
6324A-6324B: §4.62
7701(a)(30): §4.173

LABOR CODE

1986: App Q

ACTS BY POPULAR NAME
Act of July 26, 1866 (former): §11.77
Age Discrimination in Employment Act of 1967 (ADEA): §5.18
Agricultural Foreign Investment Disclosure Act of 1978: §1.89
Americans with Disabilities Act of 1990 (ADA): §§4.171, 4.173, Apps B-C, App Q
Arbitration Act: §§2.85, 2.154
Asset Conservation, Lender Liability, and Deposit Insurance Protection Act of 1996: §7.88
Bank Secrecy Act: §2.182
Civil Rights Act: §§6.98-6.100
Title VIII: §§2.181, 6.98
Title IX: §6.98
Civil Rights Act of 1866: §2.181
Clean Air Act: §1.90
Clean Water Act: §1.90
Coastal Zone Management Act: §1.90
Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA): §§1.88, 4.80, 4.173, 7.5, 7.8-7.22, 7.24-7.28, 7.30-7.31, 7.34-7.35, 7.41, 7.48, 7.61, 7.64-7.65, 7.67, 7.88, 12.1, App Q
§105: §7.15
§106: §7.17
§107: §§7.17, 7.64
§107(a): §§7.13, 7.17
§107(a)(4)(B): §7.17
§113: §7.17
§113(f): §7.17
Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA): §§5.18-5.19, App Q
Electronic Signatures in Global and National Commerce Act: §§2.47, 4.12
Employee Retirement Income Security Act of 1974 (ERISA): §5.19, App Q
Title I: §5.19, App Q
Title I, Subtitle B, Prt 3: §5.19, App Q
Title IV: §5.19, App Q
§3(3): §5.19, App Q
§406: §5.19, App Q
§4001(a)(2): §5.19, App Q
§4001(a)(3): §5.19, App Q
§4041(f): §5.19, App Q
§4043(b): §5.19, App Q
§4062(e): §5.19, App Q
§4063(a): §5.19, App Q
§4241: §5.19, App Q
Exon-Florio Amendment to the Defense Production Act of 1950: §1.89
Fair Housing Act (FHA): §§2.181, 6.98, 6.100, 6.102-6.103
Fair Housing Amendments Act of 1988: §6.98
Farm Credit Act of 1971: App A
Federal Arbitration Act (FAA): §§6.15, 6.18-6.18A
Federal Truth in Lending Act: §9.13
Flood Disaster Protection Act: §1.90
Foreign Investment in Real Property Tax Act of 1980 (FIRPTA): §§1.89, 4.132, 6.94, 9.23, 15.17, 15.80, 15.84, App Q
Garn-St. Germain Depository Institutions Act of 1982 (Garn Act): §§4.43, 9.16, 9.50-9.52
§341: §§9.50, 9.52
§341(b)(1): §4.43
Hart-Scott-Rodino Antitrust Improvements Act of 1976: §§1.67, 5.12, 5.25, App Q
Hazardous Materials Transportation Safety and Security Reauthorization Act: §4.173, App Q
Housing and Economic Recovery Act of 2008: §§6.97, 15.81
Installment Sales Revision Act of 1980: §§9.25, 9.38, 9.60
International Investment and Trade in Service Survey Act of 1976: §1.89
Michigan Leaking Underground Storage Tank Act: §7.65
Mortgage Forgiveness Debt Relief Act of 2007: §6.106F
National Environmental Policy Act of 1969 (NEPA): §1.90
National Flood Insurance Act: §§13.53, 13.130
National Housing Act: §9.54
National Labor Relations Act of 1935 (NLRA): §5.18
New York General Obligations Law §5-1311: §13.6
Noise Control Act: §1.90

Noise Pollution and Abatement Act of 1970: §1.90
Older Workers Benefit Protection Act of 1990: §5.18
Omnibus Appropriations Act: §7.88
Rails to Trails Act: §11.50
Real Estate Settlement Procedures Act of 1974 (RESPA): §§2.5, 2.8, 2.8B, 2.71, 2.135, 4.57, 6.23, 6.69, 15.74, 15.95
Residential Lead-Based Paint Reduction Act of 1992: §6.51
Resource Conservation and Recovery Act of 1976 (RCRA): §§1.88, 4.173, 7.8-7.9, 7.15, 7.19, 7.35, 7.48, 7.76, App Q
Secure and Fair Enforcement Mortgage Licensing Act of 2008 (SAFE): §2.7
Securities Act of 1933: §§2.11, 5.7
Sherman Antitrust Act: §§2.41, 2.118
Simplification Act of 1985: §9.34
Small Business Liability Relief and Brownfields Revitalization Act: §§7.22, 7.26
Superfund Amendments and Reauthorization Act of 1986: §7.5
Tax Reform Act of 1984: §9.34
Taxpayer Relief Act of 1997: §6.97
Terrorism Risk Insurance Act of 2002 (TRIA): §§13.124
§106(a)(2)(B): §13.124
Terrorism Risk Insurance Program Reauthorization Act of 2007: §13.124
Truth in Lending Act (TILA): §§2.8, 2.8B, 6.69, 9.13, 15.74
Uniform Vendor and Purchaser Risk Act: §§13.6, 13.13, App Q
Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (USA Patriot Act): §§1.59, 4.119, 4.173
§352(a): §2.182
Water Pollution Control Act: §7.8
Worker Adjustment and Retraining Notification Act (WARN Act): §§5.12, 5.18-5.19, App Q

SESSION LAWS
Pub L 110-289, 122 Stat 2911: §6.97
Pub L 110-289, 122 Stat 2654: §15.81
Pub L 110-160, 121 Stat 1839: §13.124
Pub L 110-142: §6.106F
Pub L 107-297, §101(b), 116 Stat 2322: §13.124
Pub L 107-118, 115 Stat 2368: §§7.22, 7.26
Pub L 107-118, 115 Stat 2356: §§7.22, 7.26
Pub L 107-56, 115 Stat 272: §2.182
Pub L 106-229, 114 Stat 464: §§2.47, 4.12
Pub L 105-34, 111 Stat 788: §6.97
Pub L 104-208, 110 Stat 3009: §7.88
Pub L 101-433, 104 Stat 978: §5.18
Pub L 101-235, 103 Stat 1987, 2026: §9.54
Pub L 99-499, 100 Stat 1613: §7.5
Pub L 99-121, 99 Stat 505: §9.34
Pub L 98-369, 98 Stat 494: §9.34
Pub L 97-320, 96 Stat 1469: §9.50
Pub L 96-499, 94 Stat 2682: §6.94
Pub L 96-471, 94 Stat 2247: §§9.38, 9.60
Pub L 96-471, §2, 94 Stat 2247: §9.25

EXECUTIVE ORDERS
13224: §§1.59, 4.119, 4.173

Regulations

CODE OF FEDERAL REGULATIONS

Title 12
202.14: §9.12
229.10: §4.35
590.4(5): §9.45
591.1-591.6: §§9.50-9.51
591.5(b)(2): §9.52

Title 16
460.16: §6.70
801.1-803.90: §1.67

Title 24

100.50(b): §2.181
100.75: §2.181
100.201-100.205: §6.100
200.87: §9.45
3500.1-3500.21: §§2.5, 2.8B
3500.1-3500.23: §15.95
3500.1(b)(2): §6.23
3500.7: §§6.23, 15.95
3500.7 (e)-(f): §15.95
3500.7(i): §15.95
3500.8: §§6.23, 15.95
3500.14: §2.5
3500.14(g)(1): §2.5
3500.15: §2.5

Title 31

103.170(b)(1)(vi): §2.182
501.701: §4.119

Title 38

36.4310: §9.45

Title 40

300.430(c): §7.16
312.1-312.31: §7.28
312.10(b): §§1.57, 7.28
312.20(a): §7.28
312.20(b): §7.28
312.21: §7.28
312.23: §7.28
312.24: §7.28
312.24(a): §7.86
312.25: §7.28
312.26: §7.28
312.27: §7.28
312.28: §7.28
312.29: §7.28
312.30: §7.28
312.31: §7.28
745.100-745.119: §6.51
745.101(a): §6.51
745.101(b): §6.51
745.101(c): §6.51
745.103: §6.51

Title 47

68.318(d): §2.12

FEDERAL REGISTER

73 Fed Reg 68204 (2008): §6.23
70 Fed Reg 66069-66113 (2005): §7.27
68 Fed Reg 17569 (2003): §2.182
62 Fed Reg 39009 (1997): §6.56

TREASURY REGULATIONS

1.121-3: §6.97
1.212-1(k): §1.20
1.453-4(c): §9.29
1.1031(k)-1: §4.127
1.1060-1(e)(1)(ii): §4.36
1.1234-1(a): §8.36
1.1234-1(a)-(b): §9.19
1.1445-1(g)(5): §9.23
1.1445-2(d)(2): §15.81

1.1445-3: §15.83
301.6323(i)-1(c): §4.62
301.6325-1(c): §4.62

TEMPORARY TREASURY REGULATIONS
15A.453-1(b)(3): §9.25
15A.453-1(b)(3)(i): §9.28
15A.453-1(b)(3)(ii): §§9.29, 9.60
15A.453-1(c)(1): §9.38
15A.453-1(c)(2)(i)(A): §9.38
15A.453-1(c)(2)-(4): §9.38
15A.453-1(c)(3)(i): §9.38
15A.453-1(c)(4): §9.38
15A.453-1(d)(3)(i): §9.24

Rulings

REVENUE RULINGS
82-150: §8.39
77-294: §9.109

REVENUE PROCEDURES
2000-35: §15.83

Rules and Standards

ABA MODEL RULES OF PROFESSIONAL CONDUCT
1.5(a): §§1.20-1.21
1.5(c): §§1.20-1.21
6.1: §1.20
6.2(b): §1.20

AMERICAN ARBITRATION ASSOCIATION REAL ESTATE INDUSTRY ARBITRATION RULE
19: §2.85

AMERICAN SOCIETY FOR TESTING AND MATERIALS (ASTM) STANDARDS
E1527-00: §§7.27, 7.29
E1527-05: §§7.29, 7.37
E1527-97: §7.27

NATIONAL ASSOCIATION OF REALTORS (NAR) CODE OF ETHICS
Art 17: §2.175

UNIFORM CODES AND ACTS

UNIFORM BUILDING CODE
2320.11.3: §6.52

UNIFORM COMMERCIAL CODE
6-103: §5.23
6-103(1)(a): §5.23

OUT-OF-STATE LAWS;INTERNATIONAL TREATIES

COLORADO REVISED STATUTES
§12-61-802: §2.38A

UNITED NATIONS CONVENTION ON THE RECOGNITION AND ENFORCEMENT OF FOREIGN ARBITRAL AWARDS (NEW YORK CONVENTION): §4.150

© The Regents of the University of California

Table of Cases

1119 Delaware v Continental Land Title Co. (1993) 16 CA4th 992, 20 CR2d 438: §12.7
11382 Beach Partnership v Libaw (1999) 70 CA4th 212, 82 CR2d 533: §8.30
20th Century Ins. Co. v Schurtz (2001) 92 CA4th 1188, 112 CR2d 547: §13.86
20th Century Ins. Co. v Stewart (1998) 63 CA4th 1333, 74 CR2d 492: §13.86
3550 Stevens Creek Assocs. v Barclays Bank (9th Cir 1990) 915 F2d 1355: §7.5

A

A & N Cleaners & Launderers, Inc., U.S. v (SD NY 1992) 788 F Supp 1317: §7.13
A.C. Label Co. v Transamerica Ins. Co. (1996) 48 CA4th 1188, 56 CR2d 207: §14.50
A/S Apothekernes Laboratorium v I.M.C. Chem. Group (7th Cir 1989) 873 F2d 155: §3.22
AIU Ins. Co. v Superior Court (1990) 51 C3d 807, 274 CR 820: §14.17
AM, Int'l, Inc. v International Forging Equip. (ND Ohio 1990) 743 F Supp 525: §7.61
Abari v State Farm Fire & Cas. Co. (1988) 205 CA3d 530, 252 CR 565: §13.96
Abell v Watson (1957) 155 CA2d 158, 317 P2d 159: §2.172
Abifadel v Cigna Ins. Co. (1992) 8 CA4th 145, 9 CR2d 910: §14.14A
Abrams v Motter (1970) 3 CA3d 828, 83 CR 855: §§4.3, 6.21
Acceptance Ins. Co. v Syufy Enters. (1999) 69 CA4th 321, 81 CR2d 557: §14.43
Acebo v Real Estate Educ., Research & Recovery Fund (1984) 155 CA3d 907, 202 CR 518: §2.169
Adams v Angelich (1964) 231 CA2d 258, 41 CR 767: §2.107
Adams v Murakami (1991) 54 C3d 105, 284 CR 318: §§13.118, 13.118E
Adjustrite Sys. v GAB Bus. Servs. (2d Cir 1998) 145 F3d 543: §3.16
Aerojet-General Corp. v Commercial Union Ins. Co. (2007) 155 CA4th 132, 65 CR3d 803: §14.25A
Aerojet-General Corp. v Transport Indem. Co. (1997) 17 C4th 38, 70 CR2d 118: §§14.17, 14.47-14.48
Aesthetic Specialties, Inc., In re (Bankr 9th Cir 1984) 37 BR 679: §8.28
Aetna Cas. & Sur. Co. v Merritt (9th Cir 1992) 974 F2d 1196: §14.57
Agostini, State v (1956) 139 CA2d 909, 294 P2d 769: §8.24
Agricultural Ins. Co. v Superior Court (1999) 70 CA4th 385, 82 CR2d 594: §13.119
Aim Ins. Co. v Culcasi (1991) 229 CA3d 209, 280 CR 766: §14.29
Akin v Business Title Corp. (1968) 264 CA2d 153, 70 CR 287: §15.31
Alameda Belt Line v City of Alameda (2003) 113 CA4th 15, 5 CR3d 879: §§8.14, 11.15, 11.99
Alamo Sch. Dist. v Jones (1960) 182 CA2d 180, 6 CR 272: §8.16
Alcan Aluminum Corp. v Carlsberg Fin. Corp. (9th Cir 1982) 689 F2d 815: §4.64
Alderson v Houston (1908) 154 C 1, 96 P 884: §§2.56, 2.114
Alex Robertson Co. v Imperial Cas. & Indem. Co. (1992) 8 CA4th 338, 10 CR2d 165: §14.51
Alexander v McKnight (1992) 7 CA4th 973, 9 CR2d 453: §6.31
Alexander v Security-First Nat'l Bank (1936) 7 C2d 718, 62 P2d 735: §§13.21, 13.24
Alfaro v Community Housing Improvement Sys. & Planning Ass'n (2009) 171 CA4th 1356, 89 CR3d 659: §§11.7, 11.75
Aliberti v Allstate Ins. Co. (1999) 74 CA4th 138, 87 CR2d 645: §13.95
All Points Traders, Inc. v Barrington Assocs. (1989) 211 CA3d 723, 259 CR 780: §2.10
Allen v Smith (2002) 94 CA4th 1270, 114 CR2d 898: §§8.3, 8.21
Alliance Mortgage Co. v Rothwell (1995) 10 C4th 1226, 44 CR2d 352: §§2.157, 13.31
Allied Grape Growers v Bronco Wine Co. (1988) 203 CA3d 432, 249 CR 872: §3.26
Allstate Ins. Co. v Chaney (ND Cal 1992) 804 F Supp 1219: §14.62
Allstate Ins. Co. v Interbank Fin. Servs. (1989) 215 CA3d 825, 264 CR 25: §14.71
Allstate Ins. Co. v Loo (1996) 46 CA4th 1794, 54 CR2d 541: §4.153
Alpha Beta Food Markets, Inc. v Retail Clerks Union (1955) 45 C2d 764, 291 P2d 433: §8.12
Amen v Merced County Title Co. (1962) 58 C2d 528, 25 CR 65: §§15.18-15.19, 15.22
Amerco, Inc. v Tullar (1960) 182 CA2d 336, 6 CR 71: §4.64
American Airlines, Inc. v Sheppard, Mullin, Richter & Hampton (2002) 96 CA4th 1017, 117 CR2d 685: §13.117
American Bible Soc'y v Mortgage Guar. Co. (1932) 217 C 9, 17 P2d 105: §4.22
American Cas. Co. v General Star Indem. Co. (2005) 125 CA4th 1510, 24 CR3d 34: §14.38
American Cas. Co. v Krieger (9th Cir 1999) 181 F3d 1113: §§13.23, 14.41
American Guar. & Liab. Ins. Co. v Vista Med. Supply (ND Cal 1988) 699 F Supp 787: §14.69
American Int'l Bank v Fidelity & Deposit Co. (1996) 49 CA4th 1558, 57 CR2d 567: §14.19
American Motorcycle Ass'n v Superior Court (1978) 20 C3d 578, 146 CR 182: §2.183
Amvest Mortgage Corp. v Antt (1997) 58 CA4th 1239, 68 CR2d 457: §§2.4, 2.174
Anderson v Badger (1948) 84 CA2d 736, 191 P2d 768: §§2.15, 2.153

Anderson v Broadwell (1931) 119 CA 150, 6 P2d 267: §10.30
Anderson v Fay Improvement Co. (1955) 134 CA2d 738, 286 P2d 513: §2.29
Anderson v Liberty Lobby, Inc. (1986) 477 US 242, 106 SC 2505, 91 LEd2d 202: §13.117A
Anderson v TimeWarner Telecom (2005) 129 CA4th 411, 28 CR3d 289: §11.50
Andover Land Co. v Hoffman (1968) 264 CA2d 87, 70 CR 38: §15.28
Andrews v Waldo (1928) 205 C 764, 272 P 1052: §2.107
Angell v Rowlands (1978) 85 CA3d 536, 149 CR 574: §4.12
Anthony v Enzler (1976) 61 CA3d 872, 132 CR 553: §§2.98, 8.6, 8.18, 9.53
Anthony v Snyder (2004) 116 CA4th 643, 10 CR3d 505: §§1.79, 1.83
Antonio v Hempel (1977) 71 CA3d 128, 139 CR 309: §2.169
Apablasa v Merritt & Co. (1959) 176 CA2d 719, 1 CR 500: §4.12
Appalachian Ins. Co. v Rivcom Corp. (1982) 130 CA3d 818, 182 CR 11: §13.97
Applegate v Ota (1983) 146 CA3d 702, 194 CR 331: §11.57
Arcadian Phosphates, Inc. v Arcadian Corp. (2d Cir 1989) 884 F2d 69: §§3.16, 3.20, 3.26, 3.29
Arden Group, Inc. v Burk (1996) 45 CA4th 1409, 53 CR2d 492: §8.58
Armitage v Decker (1990) 218 CA3d 887, 267 CR 399: §11.78
Armstrong v Sacramento Valley Realty Co. (1921) 52 CA 110, 198 P 217: §4.19
Armstrong World Indus., Inc. v Aetna Cas. & Sur. Co. (1996) 45 CA4th 1, 52 CR2d 690: §13.78
Arnold Palmer Golf Co. v Fuqua Indus. (6th Cir 1976) 541 F2d 584: §§3.19, 3.22
Arreola v County of Monterey (2002) 99 CA4th 722, 122 CR2d 38: §4.77
Asels v Asels (1919) 43 CA 574, 185 P 419: §4.23
Assilzadeh v California Fed. Bank (2000) 82 CA4th 399, 98 CR2d 176: §§2.127, 6.32A, 6.35
Atlantic Research Corp., U.S. v (2007) 551 US 128, 168 L Ed 2d 28, 127 S Ct 2331: §7.17
Auerbach v Great W. Bank (1999) 74 CA4th 1172, 88 CR2d 718: §§3.29-3.30
Augustine v Trucco (1954) 124 CA2d 229, 268 P2d 780: §§2.48, 2.115
Auslen v Johnson (1953) 118 CA2d 319, 257 P2d 664: §§8.11, 8.16
Austero v National Cas. Co. (1978) 84 CA3d 1, 148 CR 653, disapproved on other grounds in Egan v Mutual of Omaha Ins. Co. (1979) 24 C3d 809, 169 CR 691: §13.112
Austin v Richards (1956) 146 CA2d 436, 304 P2d 132: §2.113
Avco Community Developers, Inc. v South Coast Regional Comm'n (1976) 17 C3d 785, 132 CR 386: §§1.84, 4.86

B

B.L.M. v Sabo & Deitsch (1997) 55 CA4th 823, 64 CR2d 335: §1.15
BD Inns v Pooley (1990) 218 CA3d 289, 266 CR 815: §4.143
BMW of N. Am. v Gore (1996) 517 US 559, 134 L Ed 2d 809, 116 S Ct 1589: §§13.118A-13.118B
Babb v Weemer (1965) 231 CA2d 698, 42 CR 133: §12.18
Babb v Weemer (1964) 225 CA2d 546, 37 CR 533: §12.7
Babcock v Houston (1973) 33 CA3d 858, 109 CR 454: §2.63
Baker v Pierce (1950) 100 CA2d 224, 223 P2d 286: §11.66
Baker v Ramirez (1987) 190 CA3d 1123, 235 CR 857: §11.15
Baldassari v U.S. (1978) 79 CA3d 267, 144 CR 741: §4.62
Ball v Stephens (1945) 68 CA2d 843, 158 P2d 207: §11.77
Ballard v Titus (1910) 157 C 673, 110 P 118: §§11.45, 11.70
Banerian v O'Malley (1974) 42 CA3d 604, 116 CR 919: §13.22
Bank of America v J. A. Williams (1948) 84 CA2d 562, 191 P2d 17: §2.143
Bank of Escondido v Thomas (1895) 5 CU 94, 41 P 462: §4.65
Banville v Schmidt (1974) 37 CA3d 92, 112 CR 126: §2.143
Barcelon v Cortese (1968) 263 CA2d 517, 69 CR 657: §2.48
Barder v McClung (1949) 93 CA2d 692, 209 P2d 808: §6.31A
Bardis v Oates (2004) 119 CA4th 1, 14 CR3d 89: §13.118E
Barfield v Price (1871) 40 C 535: §4.8
Barkis v Scott (1949) 34 C2d 116, 208 P2d 367: §9.16
Barnhouse v City of Pinole (1982) 133 CA3d 171, 183 CR 881: §§2.187, 6.31A, 6.32
Baroco W., Inc. v Scottsdale Ins. Co. (2003) 110 CA4th 96, 1 CR3d 464: §14.57
Baron v Fire Ins. Exchange (2007) 154 CA4th 1184, 65 CR3d 502: §13.115
Barr v Rhoades (1969) 274 CA2d 852, 79 CR 505: §2.180
Barrett v Dawson (1998) 61 CA4th 1048, 71 CR2d 899: §6.104
Barrows v Jackson (1952) 112 CA2d 534, 247 P2d 99, aff'd (1953) 346 US 249, 97 L Ed 1586, 73 S Ct 1031: §12.20
Bartholomew v Staheli (1948) 86 CA2d 844, 195 P2d 824: §11.66
Bartley v California Ass'n of Realtors (1980) 115 CA3d 930, 173 CR 284: §2.118
Barton v Alexander Hamilton Life Ins. Co. (2003) 110 CA4th 1640, 3 CR3d 258: §13.117B
Basich v Allstate Ins. Co. (2001) 87 CA4th 1112, 105 CR2d 153: §13.117A
Bass v John Hancock Mut. Life Ins. Co. (1974) 10 C3d 792, 112 CR 195: §13.107
Basura v U.S. Home Corp. (2002) 98 CA4th 1205, 120 CR2d 328: §6.18
Bate v Marsteller (1959) 175 CA2d 573, 346 P2d 903: §§2.132, 2.139

Batson v Strehlow (1968) 68 C2d 662, 68 CR 589: §§2.5, 2.124, 2.133, 4.135
Baugh v Rogers (1944) 24 C2d 200, 148 P2d 633: §2.16
Baugh Constr. Co. v Mission Ins. Co. (9th Cir 1988) 836 F2d 1164: §14.20
Baumgartner v Meek (1954) 126 CA2d 505, 272 P2d 552: §§2.56, 2.114
Bay Shore Homes, Inc. v San Diego Trust & Sav. Bank (1969) 276 CA2d 108, 80 CR 849: §2.140
Beach v Faust (1935) 2 C2d 290, 40 P2d 822: §10.4
Beakins Moving & Storage Co. v Prudential Ins. (1985) 176 CA3d 245, 221 CR 738: §9.53
Bear Creek Planning Comm'n v Title Ins. & Trust Co. (1985) 164 CA3d 1227, 211 CR 172, disapproved on other grounds in Bay Dev., Ltd. v Superior Court (1990) 50 C3d 1012, 269 CR 720: §15.22
Beazell v Kane (1954) 127 CA2d 593, 274 P2d 224: §§2.69, 2.109, 2.119
Beazell v Schrader (1963) 59 C2d 577, 30 CR 534: §§2.47-2.49, 2.118
Beck v American Health Group Int'l (1989) 211 CA3d 1555, 260 CR 237: §§3.19-3.20, 3.27
Beeler v American Trust Co. (1944) 24 C2d 1, 147 P2d 583: §8.54
Beeler v West Am. Fin. Co. (1962) 201 CA2d 702, 20 CR 190: §2.125
Behniwal v Mix (2005) 133 CA4th 1027, 35 CR3d 320: §2.158
BellSouth Telecommunications, Inc. v W.R. Grace & Co. (2d Cir 1996) 77 F3d 603: §13.139
Bello v ABA Energy Corp. (2004) 121 CA4th 301, 16 CR3d 818: §11.50
Belshe v Hope (1995) 33 CA4th 161, 38 CR2d 917: §10.52
Benavides v State Farm Gen. Ins. Co. (2006) 136 CA4th 1241, 39 CR3d 650: §13.112
Benner v Industrial Acc. Comm'n (1945) 26 C2d 346, 159 P2d 24: §13.95
Benson v Shotwell (1890) 87 C 49, 25 P 249: §§4.68, 10.15
Bergin v Van Der Steen (1951) 107 CA2d 8, 236 P2d 613: §8.21
Bergsoe Metal Corp., In re (9th Cir 1990) 910 F2d 668: §7.88
Bergson v Builders Ins. Co. (1869) 38 C 541: §13.24
Berzon v U.L.C. Corp. (1969) 274 CA2d 690, 79 CR 277: §2.56
Bess v County of Humboldt (1992) 3 CA4th 1544, 5 CR2d 399: §11.77
Best v Wohlford (1904) 144 C 733, 78 P 293: §10.35
Betts v Allstate Ins. Co. (1984) 154 CA3d 688, 201 CR 528: §1.15
Beverage v Canton Placer Mining Co. (1955) 43 C2d 769, 278 P2d 694: §11.99
Beverly Way Assocs. v Barham (1990) 226 CA3d 49, 276 CR 240: §4.100
Bewick v Mecham (1945) 26 C2d 92, 156 P2d 757: §9.107
Biagini v Beckham (2008) 163 CA4th 1000, 78 CR3d 171: §11.77
Biakanja v Irving (1958) 49 C2d 647, 320 P2d 16: §§2.147, 2.159
Bialo v Western Mut. Ins. Co. (2002) 95 CA4th 68, 115 CR2d 3: §13.93
Bianchi v State Farm Fire & Cas. Co. (ND Cal 2000) 120 F Supp 2d 837-840: §13.53
Bias v Reed (1914) 169 C 33, 145 P 516: §10.72
Bibb, Estate of (2001) 87 CA4th 461, 104 CR2d 415: §10.31
Big Creek Lumber Co. v County of Santa Cruz (2006) 38 C4th 1139, 45 CR3d 21: §1.80
Birkhofer v Krumm (1935) 4 CA2d 43, 40 P2d 553: §4.41
Bischel v Fire Ins. Exch. (1991) 1 CA4th 1168, 2 CR2d 575: §§13.87, 13.107
Black Eagle Oil Co. v Belcher (1913) 22 CA 258, 133 P 1153: §11.91
Black Hills Invs., Inc. v Albertson's, Inc. (2007) 146 CA4th 883, 53 CR3d 263: §§1.83, 4.92, 11.24
Blackburn v Drake (1963) 211 CA2d 806, 27 CR 651: §§10.53, 10.71
Blackburn v McCoy (1934) 1 CA2d 648, 37 P2d 153: §15.16
Blackmore v Powell (2007) 150 CA4th 1593, 59 CR3d 527: §11.52
Blackwell v Atkinson (1859) 14 C 470: §12.17
Blaisdell v Leach (1894) 101 C 405, 35 P 1019: §§10.55, 10.76
Blank v Borden (1974) 11 C3d 963, 115 CR 31: §§2.54, 2.56, 2.97, 2.110, 2.114, 2.148
Blasiar, Inc. v Fireman's Fund Ins. Co. (1999) 76 CA4th 748, 90 CR2d 374: §13.74
Bleecher v Conte (1981) 29 C3d 345, 213 CR 852: §§4.149, 6.21
Blickman Turkus, LP v MF Downtown Sunnyvale, LLC (2008) 162 CA4th 858, 76 CR3d 325: §§2.178-2.179
Boerner v Colwell Co. (1978) 21 C3d 37, 145 CR 380: §9.6
Boggs v Boggs (1944) 63 CA2d 576, 147 P2d 116: §10.52
Bohannan v City of San Diego (1973) 30 CA3d 416, 106 CR 333: §4.86
Bonaparte v Allstate Ins. Co. (9th Cir 1994) 49 F3d 486: §13.25
Bond v Aickley (1914) 168 C 161, 141 P 1188: §11.91
Boquilon v Beckwith (1996) 49 CA4th 1697, 57 CR2d 503: §6.109
Borg v Transamerica Ins. Co. (1996) 47 CA4th 448, 54 CR2d 811: §14.49
Born v Koop (1962) 200 CA2d 519, 19 CR 379: §§2.106-2.107
Bosetti v U.S. Life Ins. Co. in City of New York (2009) 175 CA4th 1208, 96 CR3d 744: §13.112
Boughton v Socony Mobil Oil Co. (1964) 231 CA2d 188, 41 CR 714: §10.50
Bowen, Truman (1949) 12 TC 446, acq 1951-2 Cum Bull 1: §9.21
Bowers, People v (1964) 226 CA2d 463, 38 CR 238: §11.55
Boyce v Bumb (ND Cal 1996) 944 F Supp 807: §7.18
Boye v Boerner (1940) 38 CA2d 567, 101 P2d 757: §10.75

Boyle v Sweeney (1989) 207 CA3d 998, 255 CR 153: §9.96
Bradbury v Davenport (1896) 114 C 593, 46 P 1062: §10.41
Bradbury v Thomas (1933) 135 CA 435, 27 P2d 402: §9.100
Brady v Carman (1960) 179 CA2d 63, 3 CR 612: §§2.144, 6.31A
Brandt v Fox (1979) 90 CA3d 737, 153 CR 683: §2.171
Brandt v Superior Court (1985) 37 C3d 813, 210 CR 211: §13.115
Brasier v Sparks (1993) 17 CA4th 1756, 22 CR2d 1: §6.36
Braun v Crew (1920) 183 C 728, 192 P 531: §§4.41, 9.48
Brehm v 21st Century Ins. Co. (2008) 166 CA4th 1225, 83 CR3d 410: §13.112
Brereton v Burton (1938) 27 CA2d 464, 81 P2d 238: §10.41
Breshears v Indiana Lumbermens Mut. Ins. Co. (1967) 256 CA2d 245, 63 CR 879: §13.87
Brewer v Murphy (2008) 161 CA4th 928, 74 CR3d 436: §11.77
Brian Chuchua's Jeep, Inc. v Farmers Ins. Group (1992) 10 CA4th 1579, 13 CR2d 444: §13.86
Bright v Board of Supervisors (1977) 66 CA3d 191, 135 CR 758: §9.103
Britschgi v McCall (1953) 41 C2d 138, 257 P2d 977: §4.3
Brizuela v Calfarm Ins. Co. (2004) 116 CA4th 578, 10 CR3d 661: §13.92
Broadmoor Improvement Ass'n v Stan Weber & Assocs. (5th Cir 1979) 597 F2d 568: §2.181
Broadmoor San Clemente Homeowners Ass'n v Nelson (1994) 25 CA4th 1, 30 CR2d 316: §6.104
Broadway, Laguna, Vallejo Ass'n v Board of Permit Appeals (1967) 66 C2d 767, 59 CR 146: §4.87
Broberg v The Guardian Life Ins. Co. of Am. (2009) 171 CA4th 912, 90 CR3d 225: §13.123
Brodkin v State Farm Fire & Cas. Co. (1989) 217 CA3d 210, 265 CR 710: §§13.83, 13.86, 13.141
Brooks, Marriage of (2008) 169 CA4th 176, 86 CR3d 624: §11.11
Brooks & Robinson, Marriage of (2008) 169 CA4th 176, 86 CR3d 624: §10.2
Brown v Gordon (1966) 240 CA2d 659, 49 CR 901: §2.149
Brown v IAC (1917) 174 C 457, 163 P 664: §§2.15, 2.18
Brown v Jenson (1953) 41 C2d 193, 259 P2d 425: §4.41
Brown v Royal Maccabees Life Ins. Co. (10th Cir 1998) 137 F3d 1236: §13.107
Brown Derby Hollywood Corp. v Hatton (1964) 61 C2d 855, 40 CR 848: §4.67
Bruckman v Parliament Escrow Corp. (1987) 190 CA3d 1051, 235 CR 813: §15.22
Brudvig v Renner (1959) 172 CA2d 522, 342 P2d 276: §11.15
Bruggeman v Sokol (1954) 122 CA2d 876, 265 P2d 575: §4.83
Brumbaugh v County of Imperial (1982) 134 CA3d 556, 184 CR 11: §11.77
Bruner v Van's Mkts. (1951) 103 CA2d 135, 229 P2d 56: §§2.45, 2.48
Bryan v Ramirez (1857) 8 C 461: §10.69
Bryan v Swain (1880) 56 C 616: §4.109
Bryant v Blevins (1994) 9 C4th 47, 36 CR2d 86: §11.78
Buckaloo v Johnson (1975) 14 C3d 815, 122 CR 745, disapproved on other grounds in Della Penna v Toyota Motor Sales, U.S.A. (1995) 11 C4th 376, 45 CR2d 436: §§2.121-2.123
Buckley v Savage (1960) 184 CA2d 18, 7 CR 328: §§2.26, 2.172
Budd v Nixen (1971) 6 C3d 195, 98 CR 849: §1.14
Budget Marketing, Inc. v Centronics Corp. (8th Cir 1991) 927 F2d 421: §§3.26, 3.29
Budget Realty, Inc. v Hunter (1984) 157 CA3d 511, 204 CR 48: §9.97
Buechner v Jonas (1964) 228 CA2d 127, 39 CR 298: §11.62
Buehler v Oregon-Washington Plywood Corp. (1976) 17 C3d 520, 131 CR 394: §11.49
Builders' Control Serv. v North Am. Title Guar. Co. (1962) 205 CA2d 68, 22 CR 712: §§15.14, 15.23, 15.30, 15.93-15.94
Bullock v Philip Morris USA, Inc. (2008) 159 CA4th 655, 71 CR3d 775: §13.118A
Burch v Argus Props. (1979) 92 CA3d 128, 154 CR 485: §2.149
Burch v Gombos (2000) 82 CA4th 352, 98 CR2d 119: §11.77
Burk v Municipal Court (1964) 229 CA2d 696, 40 CR 425: §4.86
Burke v California Coastal Comm'n (2008) 168 CA4th 1098, 85 CR3d 909: §11.82
Burkett v J.A. Thompson & Son (1957) 150 CA2d 523, 310 P2d 56: §§2.184, 2.187
Burks v Poppy Constr. Co. (1962) 57 C2d 463, 20 CR 609: §6.101
Burlington N. & Santa Fe Ry. Co. v U. S. (2009) 556 US __, 173 L Ed 2d 812, 129 S Ct 1870: §7.10
Burlington N. & Santa Fe Ry. Co., U.S. v (9th Cir 2007) 479 F3d 1113, 1136 (case was consolidated and cert granted Oct. 1, 2008) 2008 US Lexis 5437, 171 L Ed 2d 931, 129 S Ct 30: §7.12
Burnaby v Standard Fire Ins. Co. (1995) 40 CA4th 787, 47 CR2d 326: §13.115
Burnand v Nowell (1948) 84 CA2d 1, 189 P2d 796: §4.109
Burnet v Logan (1931) 283 US 404, 75 L Ed 1143, 51 S Ct 550: §9.38
Burns v California Fair Plan (2007) 152 CA4th 646, 61 CR3d 809: §§13.16, 13.21A, 13.23
Business to Business Markets, Inc. v Zurich Specialties London Ltd. (2005) 135 CA4th 165, 37 CR3d 295: §14.20
Buss v Superior Court (1997) 16 C4th 35, 65 CR2d 366: §§14.17, 14.39, 14.53-14.56
Bustillos v Murphy (2002) 96 CA4th 1277, 117 CR2d 895: §11.57
Butcher v Dauz (1967) 257 CA2d 524, 65 CR 166: §9.75
Buxbaum v Aetna Life & Cas. Co. (2002) 103 CA4th 434, 126 CR2d 682: §§13.55, 13.59

C

C. Robert Nattress & Assocs. v CIDCO (1986) 184 CA3d 55, 229 CR 33: §8.24
C.H. Mead Coal Co. v Commissioner (4th Cir 1934) 72 F2d 22: §8.36
CAMSI IV v Hunter Tech. Corp. (1991) 230 CA3d 1525, 282 CR 80: §7.20
CP Holdings v Goldberg-Zoino & Assocs. (D NH 1991) 769 F Supp 432: §7.5
Caballero v Balamotis (1956) 144 CA2d 58, 300 P2d 363: §11.78
Cadillac Fairview/Cal. v Dow Chem. Co. (9th Cir 1988) 840 F2d 691: §§7.15-7.16, 7.18
Cadle Co. II v Harvey (2000) 83 CA4th 927, 100 CR2d 150: §§9.8, 9.48
Cady v Purser (1901) 131 C 552, 63 P 844: §§12.2, 15.92
Caine v Briscoe (1926) 78 CA 660, 248 P 774: §2.109
Caito v United Cal. Bank (1978) 20 C3d 694, 144 CR 751: §§10.30, 11.11, 12.7
Cal-Farm Ins. Co. v TAC Exterminators, Inc. (1985) 172 CA3d 564, 218 CR 407: §§13.74, 14.51
CalFarm Ins. Co. v Krusiewicz (2005) 131 CA4th 273, 31 CR3d 619: §14.63
Calemine v Samuelson (2009) 171 CA4th 153, 89 CR3d 495: §§2.127, 6.31, 6.32A
California v Montrose Chem. Corp. (9th Cir 1997) 104 F3d 1507: §7.20
California v Neville Chem. Co. (9th Cir 2004) 358 F3d 661: §7.22
California, U.S. v (1965) 381 US 139, 14 L Ed 2d 296, 85 S Ct 1401: §11.82
California Auto Court Ass'n v Cohn (1950) 98 CA2d 145, 219 P2d 511: §2.100
California Coastal Comm'n v Quanta Inv. Corp. (1980) 113 CA3d 579, 170 CR 263: §4.88
California Dep't of Toxic Substances Control v Celtor Chem. Corp. (ND Cal 1995) 901 F Supp 1481: §7.14
California Fair Plan Ass'n v Superior Court (2004) 115 CA4th 158, 8 CR3d 746: §13.92
California Food Serv. Corp. v Great Am. Ins. Co. (1982) 130 CA3d 892, 182 CR 67: §§3.10, 3.16, 3.18, 13.20
California Land Sec. Co. v Ritchie (1919) 40 CA 246, 180 P 625: §§2.58, 2.107
California Real Estate Loans, Inc. v Wallace (1993) 18 CA4th 1575, 23 CR2d 462: §§2.15, 2.20, 2.173
California Union Ins. Co. v Landmark Ins. Co. (1983) 145 CA3d 462, 193 CR 461: §14.49
Calvi v Bittner (1961) 198 CA2d 312, 17 CR 850: §§11.14-11.15
Cameron v Pillsbury (1916) 173 C 83, 159 P 149: §2.18
Camp Meeker Water Sys., Inc. v Public Util. Comm'n (1990) 51 C3d 845, 274 CR 678: §11.43
Campbell v Alger (1999) 71 CA4th 200, 83 CR2d 696: §§8.29, 8.58
Campbell v Genshlea (1919) 180 C 213, 180 P 336: §10.77
Canal Oil Co. v National Oil Co. (1937) 19 CA2d 524, 66 P2d 197: §10.75
Cannon v Selmser (1927) 85 CA 783, 260 P 332: §2.111
Cantu v Resolution Trust Corp. (1992) 4 CA4th 857, 6 CR2d 151: §15.98
Cardoza v Moorehouse (1961) 197 CA2d 76, 17 CR 28: §2.106
Carey v Cusack (1966) 245 CA2d 57, 54 CR 244: §§2.48-2.49
Carl E. Koch (1976) 67 TC 71, acq 1980 Cum Bull 1: §8.35
Carleton v Tortosa (1993) 14 CA4th 745, 17 CR2d 734: §§2.146, 2.147A, 2.151
Carlisle Homes, Inc., In re (Bankr D NJ 1988) 103 BR 524: §8.28
Carlsen v Zane (1968) 261 CA2d 399, 67 CR 747: §2.58
Carlson v Richardson (1968) 267 CA2d 204, 72 CR 769: §3.14
Carma Developers (Cal.), Inc. v Marathon Dev. Cal., Inc. (1992) 2 C4th 342, 6 CR2d 467: §13.112
Carpenson v Najarian (1967) 254 CA2d 856, 62 CR 687: §9.83
Carpenter v Hamilton (1936) 18 CA2d 69, 62 P2d 1397: §6.73
Carpenters Health & Welfare Trust Fund v Shafer (1983) 146 CA3d 504, 194 CR 266: §15.92
Carr v Schomberg (1951) 104 CA2d 850, 232 P2d 597: §11.78
Carroll v Carroll (1940) 16 C2d 761, 108 P2d 420: §4.16
Carson Harbor Village, Ltd. v Unocal Corp. (9th Cir 2001) 270 F3d 863: §§7.12, 7.16
Casey, In re (2008) 4 Cal St Bar Ct Rptr 11237, 2008 Cal Op Lexis Ct 3: §1.7
Cassim v Allstate Ins. Co. (2004) 33 C4th 780, 16 CR3d 374: §13.115
Cel-Tech Communications, Inc. v Los Angeles Cellular Tel. Co. (1999) 20 C4th 163, 83 CR2d 548: §13.122
Central Contra Costa Sanitary Dist. v National Sur. Corp. (1952) 112 CA2d 61, 246 P2d 150: §4.161
Central Mut. Ins. Co. v Schmidt (1957) 152 CA2d 671, 313 P2d 132: §§2.178, 4.77
Central Nat'l Ins. Co. v Superior Court (1992) 2 CA4th 926, 3 CR2d 622: §§13.82, 13.94
Central Pac. R.R. v Beal (1873) 47 C 151: §11.25
Century 21 Butler Realty, Inc. v Vasquez (1995) 41 CA4th 888, 49 CR2d 1: §2.105
Century Indem. Co. v Hearrean (2002) 98 CA4th 734, 120 CR2d 66: §14.23
Century Sur. Co. v Polisso (2006) 139 CA4th 922, 43 CR3d 468: §§13.118-13.118B, 13.118E, 13.120, 13.1118C
Certain Underwriters at Lloyd's of London v Superior Court (2001) 24 C4th 945, 103 CR2d 672: §§13.49, 14.25A
Chadwick v Fire Ins. Exch. (1993) 17 CA4th 1112, 21 CR2d 871: §§13.81, 13.83, 13.86, 13.141
Chaffee v Sorensen (1951) 107 CA2d 284, 236 P2d 851: §10.6
Chan v Tsang (1991) 1 CA4th 1578, 3 CR2d 14: §§2.119-2.120
Chapman v Farr (1982) 132 CA3d 1021, 183 CR 606: §2.9
Chapman v Gilmore (1963) 221 CA2d 506, 34 CR 515: §§2.77, 2.119
Chapman, U.S. v (9th Cir 1998) 146 F3d 1166: §7.19
Chateau Chamberay Homeowners Ass'n v Associated Int'l Ins. Co. (2001) 90 CA4th 335, 108 CR2d 776: §§13.23, 13.120

Chatton v National Union Fire Ins. Co. (1992) 10 CA4th 846, 13 CR2d 318: §14.29
Cheeks v California Fair Plan Ass'n (1998) 61 CA4th 423, 71 CR2d 568: §13.102
Chemical Waste Mgmt., Inc. v Armstrong World Indus. (ED Pa 1987) 669 F Supp 1285: §§7.18, 7.76
Chevron U.S.A. Inc. v Superior Court (1994) 44 CA4th 1009, 54 CR2d 324: §7.20
Childs v Newfield (1934) 136 CA 217, 28 P2d 924: §10.14
Chipman v Emeric (1855) 5 C 49: §4.73
Chodur v Edmonds (1985) 174 CA3d 565, 220 CR 80: §2.171
Christensen v Slawter (1959) 173 CA2d 325, 343 P2d 341: §4.109
Christian v Flora (2008) 164 CA4th 539, 78 CR3d 892: §10.2
Chrysler Capital Corp. v Southeast Hotel Prop. (SD NY 1988) 697 F Supp 794, aff'd without published opinion (2d Cir 1989) 888 F2d 1376: §§3.19, 3.21
Chu v Canadian Indem. Co. (1990) 224 CA3d 86, 274 CR 20: §14.48
Chugach Forest Prods., Inc., In re (9th Cir 1994) 23 F3d 241: §9.47
Cisco v Van Lew (1943) 60 CA2d 575, 141 P2d 433: §4.157
Citizens for Covenant Compliance v Anderson (1995) 12 C4th 345, 47 CR2d 898: §§4.66, 11.7
City & County of San Francisco v Union Pac. R.R. Co. (1996) 50 CA4th 987, 58 CR2d 1: §§10.2, 11.15, 11.49, 11.72
City of Greenville v W.R. Grace & Co. (D SC 1986) 640 F Supp 559, aff'd (4th Cir 1987) 827 F2d 975: §7.5
City of Hollister v Monterey Ins. Co. (2008) 165 CA4th 455, 81 CR3d 72: §13.103
City of Lodi v Randtron (2004) 118 CA4th 337, 13 CR3d 107: §7.15
City of Long Beach v Daugherty (1977) 75 CA3d 972, 142 CR 593: §11.77
City of Los Angeles v Pacific Elec. Ry. Co. (1959) 168 CA2d 224, 335 P2d 1042: §11.25
City of Manhattan Beach v Superior Court (1996) 13 C4th 232, 52 CR2d 82: §§10.2, 11.14-11.15, 11.31, 11.49
City of Pasadena v Porter (1927) 201 C 381, 257 P 526: §10.48
City of Santa Cruz v MacGregor (1960) 178 CA2d 45, 2 CR 727: §§3.18-3.19
City of Turlock v Paul M. Zagaris, Inc. (1989) 209 CA3d 189, 256 CR 902: §8.5
City of Venice v Short Line Beach Land Co. (1919) 180 C 447: §11.77
City of Vernon v Board of Harbor Commissioners (1998) 63 CA4th 677, 74 CR2d 497: §3.16
City of Walnut Creek v Leadership Hous. Sys. (1977) 73 CA3d 611, 140 CR 690: §§8.29, 8.32
Claremont Terrace Homeowners' Ass'n v U.S. (1983) 146 CA3d 398, 194 CR 216: §§8.1, 8.6, 8.22, 8.26
Clark v Patterson (1931) 213 C 4, 300 P 967: §2.67
Claudino v Pereira (2008) 165 CA4th 1282, 82 CR3d 464: §§11.17, 11.49
Clauser v Taylor (1941) 44 CA2d 453, 112 P2d 661: §4.77
Claussen v First Am. Title Guar. Co. (1986) 186 CA3d 429, 230 CR 749: §15.18
Cline v Yamaga (1979) 97 CA3d 239, 158 CR 598: §2.94
Cloney, Marriage of (2001) 91 CA4th 429, 110 CR2d 615: §§12.2, 15.20, 15.38
Cochran v Ellsworth (1954) 126 CA2d 429, 272 P2d 904: §§2.102, 2.108-2.111
Cohen v Adolph Kutner Co. (1918) 177 C 592, 171 P 424: §11.60
Cohen v Citizens Nat'l Trust & Sav. Bank (1956) 143 CA2d 480, 300 P2d 14: §2.187
Cohn v City of Oakland (1990) 223 CA3d 261, 272 CR 714: §10.11
Colbaugh v Hartline (1994) 29 CA4th 1516, 35 CR2d 213: §§2.93, 2.104
Cold Creek Compost, Inc. v State Farm Fire & Cas. Co. (2007) 156 CA4th 1469, 68 CR3d 216: §14.68A
Coldwell Banker & Co. v Pepper Tree Office Ctr. Assocs. (1980) 106 CA3d 272, 165 CR 51, disapproved on other grounds in Barrett v Bank of America (1986) 183 CA3d 1362, 229 CR 16: §§2.58, 2.101
Coldwell Banker Residential Brokerage Co., Inc. v Superior Court (2004) 117 CA4th 158, 11 CR3d 564: §2.178
Coleman v Mora (1968) 263 CA2d 137, 69 CR 166: §§2.54, 2.83, 2.148
Collett v Insurance Co. of the W. (1998) 64 CA4th 338, 75 CR2d 165: §14.67
Collier v Oelke (1962) 202 CA2d 843, 21 CR 140: §§11.69-11.70
Collin v American Empire Ins. Co. (1994) 21 CA4th 787, 26 CR2d 391: §14.19
Collins v Home Sav. & Loan Ass'n (1962) 205 CA2d 86, 22 CR 817: §§9.76-9.77, 9.84
Collins v Marvel Land Co. (1970) 13 CA3d 34, 91 CR 291: §8.23
Collins v Vickter Manor, Inc. (1957) 47 C2d 875, 306 P2d 783: §§2.107, 2.110
Colonial Sav. & Loan Ass'n v Redwood Empire Title Co. (1965) 236 CA2d 186, 46 CR 16: §2.23
Colony Hill v Ghamaty (2006) 143 CA4th 1156, 50 CR3d 247: §10.2
Commander Oil Corp. v Barlo Equip. Corp. (2d Cir 2000) 215 F3d 321: §7.13
Commissioner v Dill (3d Cir 1961) 294 F2d 291: §8.35
Common Wealth Ins. Sys., Inc. v Kersten (1974) 40 CA3d 1014, 115 CR 653: §§15.19, 15.22
Community Assisting Recovery, Inc. v Aegis Sec. Ins. Co. (2001) 92 CA4th 886, 112 CR2d 304: §13.102
Compagnie de Bauxites de Guinee v Insurance Co. of N. Am. (3d Cir 1983) 724 F2d 369: §13.81
Computer Sys. v IBM (1st Cir 1986) 795 F2d 1086: §§3.21, 3.23
Concord & Bay Point Land Co. v City of Concord (1991) 229 CA3d 289, 280 CR 623: §§11.15, 11.49
Conley v Matthes (1997) 56 CA4th 1453, 66 CR2d 518: §9.9
Conley v Poway Land & Inv. Co. (1965) 232 CA2d 22, 42 CR 636: §9.105
Conroy, Estate of (1907) 6 CA 741, 93 P 205: §10.61
Conservation Chem. Co., U.S. v (D Mo 1985) 619 F Supp 162): §7.15
Consolidated World Invs., Inc. v Lido Preferred Ltd. (1992) 9 CA4th 373, 11 CR2d 524: §6.22

Consolidation Coal Co. v Liberty Mut. Ins. (WD Pa 1976) 406 F Supp 1292: §14.38
Contemporary Invs. v Safeco Title Ins. Co. (1983) 145 CA3d 999, 193 CR 822: §§15.18, 15.23
Continental Baking Co. v Katz (1968) 68 C2d 512, 67 CR 761: §§11.49, 11.65
Continental Cas. Co. v Phoenix Constr. Co. (1956) 46 C2d 423, 296 P2d 801: §13.74
Continental Ins. Co. v Superior Court (1995) 37 CA4th 69, 43 CR2d 374: §13.114
Contini v Western Title Ins. Co. (1974) 40 CA3d 536, 115 CR 257: §11.75
Converse v Fong (1984) 159 CA3d 86, 205 CR 242: §6.21
Conway v Farmers Home Mut. Ins. Co. (1994) 26 CA4th 1185, 31 CR2d 883: §13.103
Coons v Gunn (1968) 263 CA2d 594, 69 CR 876: §6.31B
Cooper Cos., Inc. v Transcontinental Ins. Co. (1995) 31 CA4th 1094, 37 CR2d 508: §14.50
Cooper Indus. v Aviall Servs., Inc. (2004) 543 US 157, 160 L Ed 2d 548, 125 S Ct 577: §7.17
Copeland v Baskin Robbins U.S.A. (2002) 96 CA4th 1251, 117 CR2d 875: §§3.27-3.30
Copeland v Fairview Land & Water Co. (1913) 165 C 148, 131 P 119: §10.25
Corbett v Otts (1962) 205 CA2d 78, 22 CR 849: §6.30
Cordano v Wright (1911) 159 C 610, 115 P 227: §10.55
Cordova v 21st Century Ins. Co. (2005) 129 CA4th 89, 28 CR3d 170: §13.93
Cormac v Murphy (1922) 58 CA 366, 208 P 360: §1.57
Cornelison v Kornbluth (1975) 15 C3d 590, 125 CR 557: §§4.41-4.42, 9.48, 13.31
Corona Unified Sch. Dist. v Vejar (1958) 165 CA2d 561, 332 P2d 294: §4.13
Cortez v Purolator Air Filtration Prods., Co. (2000) 23 C4th 163, 96 CR2d 518: §13.122
Cory v Villa Props. (1986) 180 CA3d 592, 225 CR 628: §§2.178, 4.112
Cose v Getty Oil Co. (9th Cir 1993) 4 F3d 700: §7.8
Costanzo v Ganguly (1993) 12 CA4th 1085, 16 CR2d 55: §9.55
Cottingham v Smith (1938) 28 CA2d 345, 82 P2d 479: §2.107
Coulter v Howard (1927) 203 C 17, 262 P 751: §2.108
County of Kern, People v (1974) 39 CA3d 830, 115 CR 67: §4.86
County of Los Angeles v Berk (1980) 26 C3d 201, 161 CR 742: §11.77
County of Orange v Chandler-Sherman Corp. (1976) 54 CA3d 561, 126 CR 765: §11.77
County of San Bernardino v Pacific Indem. Co. (1997) 56 CA4th 666, 65 CR2d 657: §14.48
County of San Diego v Ace Prop. & Cas. Ins. Co. (2005) 37 C4th 406, 33 CR3d 583: §§13.49, 14.25A
County of San Diego v Miller (1975) 13 C3d 684, 119 CR 491: §§8.1, 8.5, 8.27, 8.29
County of San Diego v Miller (1980) 102 CA3d 424, 162 CR 480: §8.29
County of Solano v Handlery (2007) 155 CA4th 566, 66 CR3d 201: §10.2
County of Trinity v Rourke (1969) 275 CA2d 628, 79 CR 902: §10.16
Cox v Schnerr (1916) 172 C 371, 156 P 509: §10.77
Cox, In re (1970) 3 C3d 205, 90 CR 24: §6.101
Craig v Zelian (1902) 137 C 105, 69 P 853: §10.35
Crane v State Farm Fire & Cas. Co. (1971) 5 C3d 112, 95 CR 513: §14.82
Crawford v Weather Shield Mfg., Inc. (2008) 44 C4th 541, 79 CR3d 721: §§13.123, 14.53
Crest Mar Owners Ass'n v Stapakis (2007) 157 CA4th 1223, 69 CR3d 231: §11.112
Crimmins v Gould (1957) 149 CA2d 383, 308 P2d 786: §11.61
Crist v Fife (1919) 41 CA 509, 183 P 197: §12.14
Crittenden v McCloud (1951) 106 CA2d 42, 234 P2d 642: §10.76
Crogan v Metz (1956) 47 C2d 398, 303 P2d 1029: §§2.134-2.135, 2.162
Crookall v Davis, Punelli, Keathley & Willard (1998) 65 CA4th 1048, 77 CR2d 250: §§9.9, 9.97
Crouse-Prouty v Rogers (1917) 33 CA 246, 164 P 901: §11.91
Crowell v Issacs (1965) 235 CA2d 755, 45 CR 566: §2.83
Cumings v Hokr (1948) 31 C2d 844, 193 P2d 742: §4.66
Cummins v Gates (1965) 235 CA2d 532, 45 CR 417: §9.76
Cunningham v Security Title Ins. Co. (1966) 241 CA2d 626, 50 CR 724: §15.20
Cunningham v Universal Underwriters (2002) 98 CA4th 1141, 120 CR2d 162: §14.25
Curran v Heslop (1953) 115 CA2d 476, 252 P2d 376: §6.31A
Cushman v Davis (1978) 80 CA3d 731, 145 CR 791: §§11.57, 11.66

D

D-K Inv. Corp. v Sutter (1971) 19 CA3d 537, 96 CR 830: §8.21
DMC, Inc. v Downey Sav. & Loan Ass'n (2002) 99 CA4th 190, 120 CR2d 761: §§9.55, 9.67
Dale v Palmer (1951) 106 CA2d 663, 235 P2d 650: §2.63
Dale v Raines (1953) 115 CA2d 309, 252 P2d 22: §2.111
Dalrymple v United Servs. Auto. Ass'n (1995) 40 CA4th 497, 46 CR2d 845: §13.112
Daluiso v Boone (1969) 269 CA2d 253, 75 CR 287: §11.14
Dang, Paul Trans, TC Memo 1999-233: §9.59
Danielson v Neal (1913) 164 C 748, 130 P 716: §10.77
Danielson v Sykes (1910) 157 C 686, 109 P 87: §§11.24, 11.46
Darr v Lone Star Indus., Inc. (1979) 94 CA3d 895, 157 CR 90: §11.43

Dart Industries, Inc. v Commercial Union Ins. Co. (2002) 28 C4th 1059, 1074 n 5, 124 CR2d 142, 52 P3d 79: §14.49B
Daum v Superior Court (1964) 228 CA2d 283, 39 CR 443: §2.114
David Dobrich (1997) TC Memo 1997-477: §9.109
Davis v Chipman (1930) 210 C 609, 293 P 40: §2.94
Davis v Farmers Ins. Group (2005) 134 CA4th 100, 35 CR3d 738: §14.85
Davis v Harris (1998) 61 CA4th 507, 71 CR2d 591: §2.167
Davis v McGrew (1889) 82 C 135, 23 P 41: §10.23
Davis v Phoenix Ins. Co. (1896) 111 C 409, 43 P 1115: §§13.16-13.18, 13.21, 13.99
Davis v United Servs. Auto. Ass'n (1990) 223 CA3d 1322, 273 CR 224: §§13.86, 13.141
Davis v Ward (1895) 109 C 186, 41 P 1010: §§10.42, 15.87
Dawson v Goff (1954) 43 C2d 310, 273 P2d 1: §8.53
Dawson v Toledano (2003) 109 CA4th 387, 134 CR2d 689: §1.14
Day v City of Glendale (1975) 51 CA3d 817, 124 CR 569: §4.95
Day v Rosenthal (1985) 170 CA3d 1125, 217 CR 89: §1.15
De La Questa v Armstrong Holdings Co. (1920) 48 CA 487, 192 P 135: §2.115
de St. Germain v Watson (1950) 95 CA2d 862, 214 P2d 99: §2.172
DeBerard Props. v Lim (1999) 20 C4th 659, 85 CR2d 292: §§9.8, 9.48, 9.72, 9.97
DeBruyn v Superior Court (2008) 158 CA4th 1213, 70 CR3d 652: §§13.83, 13.130
DeWitt v Western Pac. R.R. (9th Cir 1983) 719 F2d 1448: §7.66
Dea v Davy (1957) 150 CA2d 435, 309 P2d 894: §2.107
Deas v Knapp (1981) 29 C3d 69, 171 CR 823: §2.166
Deeble v Stearns (1947) 82 CA2d 296, 186 P2d 173: §2.108
Deeter v Angus (1986) 179 CA3d 241, 224 CR 801: §2.123
Delbon v Brazil (1955) 134 CA2d 461, 285 P2d 710: §§2.81, 2.116-2.117
Delgado v Interins. Exch. of the Auto. Club of S. Cal. (2009) 47 C4th 302, 97 CR3d 298: §§14.18, 14.20, 14.53, 14.55
Della Penna v Toyota Motor Sales, U.S.A. (1995) 11 C4th 376, 45 CR2d 436: §2.122
Delos v Farmers Group, Inc., (1979) 93 CA3d 642, 155 CR 843: §13.114
Dennis v Overholtzer (1960) 178 CA2d 766, 3 CR 193, disapproved on other grounds in Ellis v Mihelis (1963) 60 C2d 206, 32 CR 415: §4.71
Derish v San Mateo-Burlingame Bd. of Realtors (1982) 136 CA3d 534, 186 CR 390: §2.41
Develop-Amatic Eng'g v Republic Mortgage Co. (1970) 12 CA3d 143, 91 CR 193: §8.54
Devereaux v Harper (1962) 210 CA2d 519, 26 CR 837: §2.109
Devin v United Servs. Auto. Ass'n (1992) 6 CA4th 1149, 8 CR2d 263: §14.22
Devonwood Condominium Owners Ass'n v Farmers Ins. Exch. (2008) 162 CA4th 1498, 77 CR3d 88: §13.97
Diamond Heights Homeowners Ass'n v National Am. Ins. Co. (1991) 227 CA3d 563, 277 CR 906: §14.63
Diamond Woodworks, Inc. v Argonaut Ins. Co. (2003) 109 CA4th 1020, 135 CR2d 736: §§13.117, 13.118B, 14.41
Diepenbrock v Luiz (1911) 159 C 716, 115 P 743: §4.73
Dill, Commissioner v (3d Cir 1961) 294 F2d 291: §8.35
Dixon v Salvation Army (1983) 142 CA3d 463, 191 CR 111: §13.3
Dobosz v State Farm Fire & Cas. Co. (Ill Ct App 1983) 458 NE2d 611: §13.107
Dobrich, David, (1997) TC Memo 1997-477: §9.109
Doctor's Assocs., Inc. v Casarotto (1996) 517 US 681, 134 L Ed 2d 902, 116 S Ct 1652: §§2.85, 6.18
Doheny W. Homeowners' Ass'n v American Guar. & Liab. Ins. Co. (1997) 60 CA4th 400, 70 CR2d 260: §13.86
Doll v Grand Union Co. (11th Cir 1991) 925 F2d 1363: §3.26
Doll v Maravilas (1947) 82 CA2d 943, 187 P2d 885: §4.73
Domarad v Fisher & Burke (1969) 270 CA2d 543, 76 CR 529: §2.51
Dombalian v Fox (1979) 88 CA3d 763, 152 CR 86: §2.169
Donnellan v Rocks (1972) 22 CA3d 925, 99 CR 692: §§2.120, 2.132
Donze v Donze (1928) 88 CA 769, 264 P 294: §10.39
Doryon v Salant (1977) 75 CA3d 706, 142 CR 378: §4.3
Dougery v Bettencourt (1931) 214 C 455, 6 P2d 499: §15.92
Doyle v Surety Title & Guar. Co. (1968) 261 CA2d 525, 68 CR 177: §9.100
DuRoss v Trainor (1932) 122 CA 732, 10 P2d 763: §15.89
Duff v Randall (1897) 116 C 226, 48 P 66: §10.77
Duffy v Cavalier (1989) 215 CA3d 1517, 264 CR 740: §2.132
Duin v Security First Nat'l Bank (1955) 132 CA2d Supp 904, 283 P2d 790: §2.141
Dunne v Colomb (1923) 192 C 740, 221 P 912: §2.110
Durfee v Garvey (1889) 78 C 546, 21 P 302: §11.66

E

E.A. Strout W. Realty v Gregoire (1950) 101 CA2d 512, 225 P2d 585: §§2.56, 2.58
E.A. Strout W. Realty Agency, Inc. v Lewis (1967) 255 CA2d 254, 62 CR 918: §§2.81, 2.100, 2.116
EOTT Energy Corp. v Storebrand Int'l Ins. Co. (1996) 45 CA4th 565, 52 CR2d 894: §13.86
Early v Owens (1930) 109 CA 489, 293 P 136: §15.20
East Hilton Drive Homeowners' Ass'n v Western Real Estate Exch., Inc. (1982) 136 CA3d 630, 186 CR 267: §§6.9, 6.30

Eastman v Piper (1924) 68 CA 554, 229 P 1002: §11.68
Easton v Montgomery (1891) 90 C 307, 27 P 280: §§4.53, 4.122
Easton v Strassburger (1984) 152 CA3d 90, 199 CR 383: §§2.150, 2.153, 2.159, 2.179, 2.183, 6.72, 11.11
Eaton v Yount (1920) 48 CA 221, 191 P 1009: §2.5
Economy Lumber Co. v Insurance Co. of N. Am. (1984) 157 CA3d 641, 204 CR 135: §14.26
Edens v Stoddard (1954) 126 CA2d 56, 271 P2d 610: §2.59
Edmonds v Augustyn (1987) 193 CA3d 1056, 238 CR 704: §2.169
Edwards v City of Santa Paula (1956) 138 CA2d 375, 292 P2d 31: §10.35
Edwards v Sergi (1934) 137 CA 369, 30 P2d 541: §4.59
Egan v Mutual of Omaha Ins. Co. (1979) 24 C3d 809, 169 CR 691: §§13.112, 13.117B
Eldridge v Burns (1982) 136 CA3d 907, 186 CR 784: §§9.100, 9.102, 9.105
Elliott v McCombs (1941) 17 C2d 23, 109 P2d 329: §10.44
Elrod, Johnie Vaden (1986) 87 TC 1046: §§8.35, 8.39
Elysian Inv. Group v Stewart Title Guar. Co. (2002) 105 CA4th 315, 129 CR2d 372: §§11.10, 12.1, 12.7, 12.12
Empire Fire & Marine Ins. Co. v Bell (1997) 55 CA4th 1410, 64 CR2d 749: §14.41
Employers Ins. of Wausau v California Water Serv. Co. (ND Cal, Aug. 25, 2008, No. C-06-03002 RMW) 2008 US Dist Lexis 65433: §14.62
Enea v Coldwell Banker/Del Monte Realty (Bankr ND Cal 1998) 225 BR 715: §2.48
England, Estate of (1991) 233 CA3d 1, 284 CR 361: §6.88
Erich v Granoff (1980) 109 CA3d 920, 167 CR 538: §§8.1, 8.5
Ernie v Trinity Lutheran Church (1959) 51 C2d 702, 336 P2d 525: §11.78
Ernst v Searle (1933) 218 C 233, 22 P2d 715: §2.42
Ertell v Lloyd's Food Prods. (1953) 115 CA2d 615, 252 P2d 683: §2.114
Escrow Agents' Fid. Corp. v Superior Court (1992) 4 CA4th 491, 5 CR2d 698: §15.4
Escrow Inst. v Pierno (1972) 24 CA3d 361, 100 CR 880: §15.6
Esicorp, Inc. v Liberty Mut. Ins. Co. (8th Cir 2001) 266 F3d 859: §14.27
Esquer v Teresi (1951) 105 CA2d 89, 232 P2d 895: §2.18
Essex Ins. Co. v BloomSouth Flooring Corp. (1st Cir 2009) 562 F3d 399: §13.139
Essex Ins. Co. v City of Bakersfield (2007) 154 CA4th 696, 65 CR3d 1: §14.53
Essex Ins. Co. v Five Star Dye House, Inc. (2006) 38 C4th 1252, 45 CR3d 362: §13.115
Essick v City of Los Angeles (1950) 34 C2d 614, 213 P2d 492: §4.87
Estate of _____ (*see* name of decedent)
Evans v Faught (1965) 231 CA2d 698, 42 CR 133: §§4.50, 4.111, 10.56, 12.7, 12.12, 12.14
Evans v Faught (1964) 225 CA2d 546, 37 CR 533: §12.18
Everett v State Farm Gen. Ins. Co. (2008) 162 CA4th 649, 75 CR3d 812: §§13.102-13.103, 13.106
Everts v Matteson (1942) 21 C2d 437, 132 P2d 476: §4.41
Exxess Elecronixx v Heger Realty Corp. (1998) 64 CA4th 698, 75 CR2d 376: §2.127
Exxon Shipping Co. v Baker (2008) __ US __, 171 L Ed 2d 570, 128 S Ct 2605: §13.118B

F

F & H Constr. v ITT Hartford Ins. Co. (2004) 118 CA4th 364, 12 CR3d 896: §§14.25-14.27, 14.63
FDIC v Jackson-Shaw Partners No. 46, Ltd. (ND Cal 1994) 850 F Supp 839: §7.20
FMC Corp. v Plaisted & Cos. (1998) 61 CA4th 1132, 72 CR2d 467: §14.47
FSR Brokerage, Inc. v Superior Court (1995) 35 CA4th 69, 41 CR2d 404: §§2.178-2.179
Fahrenbaker v E. Clemens Horst Co. (1930) 209 C 7, 284 P 905: §10.44
Fairbanks v Superior Court (2009) 46 C4th 56, 92 CR3d 279: §13.123
Faith v Meisetschlager (1919) 45 CA 7, 187 P 61: §2.58
Far W. Fin. Corp. v D & S Co. (1988) 46 C3d 796, 251 CR 202: §2.183
Far W. Sav. & Loan Ass'n v McLaughlin (1988) 201 CA3d 67, 246 CR 872: §§15.20, 15.91
Farmers Ins. Co. v Trutanich (Or App 1993) 123 Or App 6, 858 P2d 1332: §13.139
Farmland Irrig. Co. v Dopplmaier (1957) 48 C2d 208, 308 P2d 732: §4.155
Faus v City of Los Angeles (1967) 67 C2d 350, 62 CR 193: §§11.50, 11.74
Faus v Nelson (1966) 241 CA2d 320, 50 CR 483: §§11.31, 11.103
Federal Deposit Ins. Corp. v Superior Court (1997) 54 CA4th 337, 62 CR2d 713: §§10.17, 10.64
Feinberg v Intrastate Escrow Corp. (1963) 216 CA2d 80, 30 CR 781: §15.23
Feldman v Sacramento Bd. of Realtors (1981) 119 CA3d 739, 174 CR 231: §2.41
Fellom v Adams (1969) 274 CA2d 855, 79 CR 633: §§2.47, 2.94
Fibreboard Corp. v Hartford Acc. & Indem. Co. (1993) 16 CA4th 492, 20 CR2d 376: §§14.43, 14.69
Fidelity & Deposit Co. v Charter Oak Fire Ins. Co. (1998) 66 CA4th 1080, 78 CR2d 429: §14.32
Fidelity Nat'l Title Ins. Co. v Miller (1989) 215 CA3d 1163, 264 CR 17: §4.55
Fidler v Schiller (1963) 212 CA2d 569, 28 CR 48: §2.53
Field v Century 21 Klowden-Forness Realty (1998) 63 CA4th 18, 73 CR2d 784: §§2.24, 2.89, 2.128, 2.178
Fine v Southern Cal. Bus. Sales (1987) 190 CA3d 480, 235 CR 489: §2.170
Finkbohner v Glens Falls Ins. Co. (1907) 6 CA 379, 92 P 318: §13.8
Finn v Continental Ins. Co. (1990) 218 CA3d 69, 267 CR 22: §13.86

Finn v Goldstein (1927) 201 C 605, 258 P 85: §11.15
Fire Ins. Exch. v Altieri (1991) 235 CA3d 1352, 1 CR2d 360: §14.35
Fire Ins. Exch. v Jiminez (1986) 184 CA3d 437, 229 CR 83: §14.82
Fire Ins. Exch. v Superior Court (2004) 116 CA4th 446, 10 CR3d 617: §§13.69, 13.71, 13.73, 13.87, 13.103
Fireman's Fund Ins. Co. v Allstate Ins. Co. (1991) 234 CA3d 1154, 286 CR 146: §13.113
Fireman's Fund Ins. Cos. v Atlantic Richfield Co. (2001) 94 CA4th 842, 115 CR2d 26: §14.43
First Fid. Thrift & Loan Ass'n v Alliance Bank (1998) 60 CA4th 1433, 71 CR2d 295: §10.2
Fisher v County of Alameda (1993) 20 CA4th 120, 24 CR2d 384: §6.95
Fisher v Losey (1947) 78 CA2d 121, 177 P2d 334: §§2.127, 2.138
Fitzpatrick v Underwood (1941) 17 C2d 722, 112 P2d 3: §2.101
Flanagan v San Marco Silt Co. (1951) 106 CA2d 458, 235 P2d 107: §11.62
Fleet Factors Corp., U.S. v (11th Cir 1990) 901 F2d 1550: §7.88
Fleming v Dolfin (1931) 214 C 269, 4 P2d 776: §2.58
Fletcher v Stapleton (1932) 123 CA 133, 10 P2d 1019: §11.60
Flick v Liberty Mut. Fire Ins. Co. (9th Cir 2000) 205 F3d 386: §13.53
Flickenger v IAC (1919) 181 C 425, 184 P 851: §2.18
Florida Dep't of Revenue v Piccadilly Cafeterias, Inc. (2008) ___ US ___, 171 L Ed 2d 203, 128 S Ct 2326: §4.134
Floyd J. Voight (1977) 68 TC 99, aff'd (5th Cir 1980) 614 F2d 94: §9.59
Flyer's Body Shop Profit Sharing Plan v Ticor Title Ins. Co. (1986) 185 CA3d 1149, 230 CR 276: §15.23
Flynn v Mikelian (1962) 208 CA2d 305, 25 CR 138: §10.48
Food Pro Int'l v Farmers Ins. Exchange (2008) 169 CA4th 976, 89 CR3d 1: §§13.117-13.117A, 14.71
Foorman v Wallace (1888) 75 C 552, 17 P 680: §10.68
Foote v Posey (1958) 164 CA2d 210, 330 P2d 651: §2.52
Foothill Village Homeowners Ass'n v Bishop (1999) 68 CA4th 1364, 81 CR2d 195: §§13.23, 13.27
Ford v Cournale (1973) 36 CA3d 172, 111 CR 334: §2.142
Forde v Vernbro Corp. (1963) 218 CA2d 405, 32 CR 577: §9.107
Fourth La Costa Condominium Owners Ass'n v Seith (2008) 159 CA4th 563, 71 CR3d 299: §10.2
Fowler v Ross (1983) 142 CA3d 472, 191 CR 183: §4.152
Fowler v Smith (1852) 2 C 39, appeal at 2 C 568: §12.17
Frabotta v Alencastre (1960) 182 CA2d 679, 6 CR 536: §4.53
Fragale v Faulkner (2003) 110 CA4th 229, 1 CR3d 616: §§2.155, 2.157
Fraley v Allstate Ins. Co. (2000) 81 CA4th 1282, 97 CR2d 386: §13.103
Fraley v Allstate Ins. Co. 81 CA4th 1282, 97 CR2d 386: §13.120
Franceschi v Kuntz (1967) 253 CA2d 1041, 61 CR 810: §11.69
Frangipani v Boecker (1998) 64 CA4th 860, 75 CR2d 407: §9.55
Frank Lyon Co. v U.S. (1978) 435 US 561, 55 L Ed 2d 550, 98 S Ct 1291: §§9.19-9.21
Franklin v Hansen (1963) 59 C2d 570, 30 CR 530: §2.45
Fraser v Bentel (1911) 161 C 390, 119 P 509: §§12.14, 12.18
Fratt v Whittier (1881) 58 C 126: §10.44
Freedman v Queen Ins. Co. (1961) 56 C2d 454, 15 CR 69: §13.74
Freedman v State Farm Ins. Co. (2009) 173 CA4th 957, 93 CR3d 296: §§13.83, 13.86, 13.130, 13.141
Freedman v State Farm Ins. Co. (2009) 173 CA4th 957, 959 n1, 93 CR3d 296: §§13.71-13.72
Freedman v The Rector (1951) 37 C2d 16, 230 P2d 629: §9.16
Freeman v Affiliated Prop. Craftsmen (1968) 266 CA2d 723, 72 CR 357: §11.31
Freeman v Bellegarde (1895) 108 C 179, 41 P 289: §11.31
Freeman v San Diego Ass'n of Realtors (9th Cir 2003) 322 F3d 1133: §2.41
Frei v Davey (2004) 124 CA4th 1506, 22 CR3d 429: §§2.153A, 6.19
French v Brinkman (1963) 60 C2d 547, 35 CR 289: §§11.48, 11.78-11.79
French v Mortgage Guar. Co. (1940) 16 C2d 26, 104 P2d 655: §9.45
Fresno Economy Import Used Cars, Inc. v United States Fid. & Guar. Co. (1977) 76 CA3d 272, 142 CR 681: §13.74
Friedman Prof. Management Co., Inc. v Norcal Mut. Ins. Co. (2004) 120 CA4th 17, 15 CR3d 359: §14.55
Friends of "B Street v City of Hayward (1980) 106 CA3d 988, 165 CR 514: §1.76
Friends of Lake Arrowhead v Board of Supervisors (1974) 38 CA3d 497, 113 CR 539: §§4.92, 9.103
Friends of the Trail v Blasius (2000) 78 CA4th 810, 93 CR2d 193: §11.77
Friery v Sutter Buttes Sav. Bank (1998) 61 CA4th 869, 72 CR2d 32: §9.88
Fries v Broadway Fed. Sav. & Loan Ass'n (1968) 258 CA2d 119, 65 CR 460: §9.85
Fristoe v Drapeau (1950) 35 C2d 5, 215 P2d 729: §11.54
Froid v Fox (1982) 132 CA3d 832, 183 CR 461: §2.169
Frontier Oil Corp. v RLI Ins. Co. (2007) 153 CA4th 1436, 63 CR3d 816: §§14.37, 14.53, 14.55
Fry v George Elkins Co. (1958) 162 CA2d 256, 327 P2d 905: §§4.3, 4.83
Fudickar v East Riverside Irrig. Dist. (1895) 109 C 29, 41 P 1024: §11.15
Fugate v Cook (1965) 236 CA2d 700, 46 CR 291: §4.12
Fujita, People v (1932) 215 C 166, 8 P2d 1011: §4.15
Furla v Jon Douglas Co. (1998) 65 CA4th 1069, 76 CR2d 911: §§2.178, 6.72

G

Gaffey v Welk (1920) 46 CA 385, 189 P 300: §12.13
Gagne v Bertran (1954) 43 C2d 481, 275 P2d 15: §2.184
Gaither v Gaither (1958) 165 CA2d 782, 332 P2d 436: §11.66
Galdjie v Darwish (2003) 113 CA4th 1331, 7 CR3d 178: §§4.152, 10.19, 15.26, 15.59, 15.97
Gans v Smull (2003) 111 CA4th 985, 4 CR3d 353: §4.152
Garamendi v Golden Eagle Ins. Co. (2005) 127 CA4th 480, 25 CR3d 642: §13.86
Garcia v Roberts (2009) 173 CA4th 900, 93 CR3d 286: §9.19
Gardner v County of Sonoma (2003) 29 C4th 990, 129 CR2d 869: §11.24
Gardner v Murphy (1975) 54 CA3d 164, 126 CR 302: §2.183
Garver v Brace (1996) 47 CA4th 995, 55 CR2d 220: §9.30
Garvey v State Farm Fire & Cas. Co. (1989) 48 C3d 395, 257 CR 292: §§13.71-13.73, 13.76, 13.83-13.84
Gates Rubber Co. v Ulman (1989) 214 CA3d 356, 262 CR 630: §§8.22, 11.11, 12.7
Gatley v Shockley (1932) 215 C 604, 12 P2d 436: §8.25
Geddes & Smith, Inc. v St. Paul Mercury Indem. Co. (1959) 51 C2d 558, 334 P2d 881: §§14.26, 14.65
Gee v Moore (1859) 14 C 472: §12.9
Geernaert v Mitchell (1995) 31 CA4th 601, 37 CR2d 483: §§2.178, 2.187, 4.49
General Elec. Co. v EPA (DC Cir 2004) 360 F3d 188: §7.15
General Ins. Co. v Pathfinder Petroleum Co. (9th Cir 1944) 145 F2d 368: §§13.55, 13.61
George F. Hillenbrand, Inc. v Insurance Co. of N. Am. (2002) 104 CA4th 784, 128 CR2d 586: §§14.24, 14.65
Gerhard v Stephens (1968) 68 C2d 864, 69 CR 612: §§11.62, 11.80
Ghirardo v Antonioli (1994) 8 C4th 791, 35 CR2d 418: §9.6
Gibbo v Berger (2004) 123 CA4th 396, 19 CR3d 829: §2.9
Gifford v Roberts (1947) 81 CA2d 712, 184 P2d 942: §6.73
Gilardi v Hallam (1981) 30 C3d 317, 178 CR 624: §§11.57, 11.77
Gill v Mission Sav. & Loan Ass'n (1965) 236 CA2d 753, 46 CR 456: §9.85
Gillis v Sun Ins. Office, Ltd. (1965) 238 CA2d 408, 47 CR 868: §13.25
Gion v City of Santa Cruz (1970) 2 C3d 29, 84 CR 162: §11.77
Gipson v Davis Realty Co. (1963) 215 CA2d 190, 30 CR 253: §§2.15, 2.20
Gladstone, Realtors v Bellwood (1979) 441 US 91, 60 L Ed 2d 66, 99 S Ct 1601: §2.181
Glatts v Henson (1948) 31 C2d 368, 188 P2d 745: §11.64
Glavinich v Commonwealth Land Title Ins. Co. (1984) 163 CA3d 263, 209 CR 266: §15.87
Glendale Bd. of Realtors v Hounsell (1977) 72 CA3d 210, 139 CR 830: §§2.41, 2.118
Globe Indem. Co. v Superior Court (1992) 6 CA4th 725, 8 CR2d 251: §13.92
Gluskin v Atlantic Sav. & Loan Ass'n (1973) 32 CA3d 307, 108 CR 318: §9.88
Glynn v Marquette (1984) 152 CA3d 277, 199 CR 306: §4.153
Goad v Moulton (1885) 67 C 536, 8 P 63: §10.13
Godfrey v Steinpress (1982) 128 CA3d 154, 180 CR 95: §§6.31A, 6.59
Gogerty v General Acc., Fire & Life Assur. Corp. (1965) 238 CA2d 574, 48 CR 37: §14.20
Goia, Marriage of (2004) 119 CA4th 272, 14 CR3d 362: §10.4
Golden v Anderson (1967) 256 CA2d 714, 64 CR 404: §2.121
Golden Eagle Ins. Co. v Insurance Co. of the W. (2002) 99 CA4th 837, 121 CR2d 682: §14.51
Golden Eagle Ins. Co. v Travelers Cos. (9th Cir 1996) 103 F3d 750: §14.65
Golden Eagle Ins. Corp. v Cen-Fed, Ltd. (2007) 148 CA4th 976, 56 CR3d 279: §§14.25, 14.69
Goldstein v Hensley (1906) 4 CA 444, 88 P 507: §12.14
Goodwest Rubber Corp. v Munoz (1985) 170 CA3d 919, 216 CR 604: §§8.1, 8.14
Gordon v City of San Diego (1895) 108 C 264, 41 P 301: §10.53
Gould v Wise (1893) 97 C 532, 32 P 576: §10.76
Gourley v State Farm Mut. Auto. Ins. Co. (1991) 53 C3d 121, 3 CR2d 666: §13.114
Grabau v Brown (In re Grabau) (Bankr ND Cal 1993) 151 BR 227: §2.171
Graff v Middleton (1872) 43 C 341: §12.22
Grand v Griesinger (1958) 160 CA2d 397, 325 P2d 475: §2.13
Grand Grove of United Ancient Order of Druids v Garibaldi Grove No. 71 (1900) 130 C 116, 62 P 486: §10.16
Grant v Marinell (1980) 112 CA3d 617, 169 CR 414: §2.52
Grant v Ratliff (2008) 164 CA4th 1304, 79 CR3d 902: §11.77
Grant v Woods (1977) 71 CA3d 647, 139 CR 533: §2.17
Gravillis v Coldwell Banker Residential Brokerage Co. (2006) 143 CA4th 761, 49 CR3d 531: §6.17
Gray v Don Miller & Assocs. (1984) 35 C3d 498, 198 CR 551: §2.158
Gray v McCormick (2009) 167 CA4th 1019, 84 CR3d 777: §11.52
Gray v Zurich Ins. Co. (1966) 65 C2d 263, 54 CR 104: §§14.17, 14.53-14.55
Great American Ins. Co. of New York v North American Specialty Ins. Co. (D Nev 2008) 542 F Supp 2d 1203: §14.49B
Great Northern Ry. v U.S. (1942) 315 US 262, 86 L Ed 836, 62 S Ct 529: §11.71
Greco v Oregon Mut. Fire Ins. Co. (1961) 191 CA2d 674, 12 CR 802: §13.24
Green v Skinner (1921) 185 C 435, 197 P 60: §10.75
Greene v Municipal Court (1975) 51 CA3d 446, 124 CR 139: §9.16

Greenzweight v Title Guar. & Trust Co. (1934) 1 C2d 577, 36 P2d 186: §15.27
Griffin Dewatering Corp. v Northern Ins. Co. of New York (2009) 176 CA4th 172, 97 CR3d 568: §§14.53, 14.55, 14.68A
Grigsby, Estate of (1982) 134 CA3d 611, 184 CR 886: §§6.87, 10.57
Gronenschild v Ritzenthaler (1947) 81 CA2d 138, 183 P2d 720: §8.54
Grothe v Cortlandt Corp. (1992) 11 CA4th 1313, 15 CR2d 38: §6.87
Gruenberg v Aetna Ins. Co. (1973) 9 C3d 566, 108 CR 480: §§13.112, 13.116
Guidice v BFG Electroplating & Mfg. Co. (WD Pa 1989) 732 F Supp 556: §7.88
Guttenberger v Woods (1876) 51 C 523: §4.65
Gwin v Calegaris (1903) 139 C 384, 73 P 851: §4.68

H

Haggard v Commissioner (9th Cir 1956) 241 F2d 288: §9.20
Hagge v Drew (1945) 27 C2d 368, 165 P2d 461: §15.28
Haigler v Donnelly (1941) 18 C2d 674, 117 P2d 331: §§2.61, 2.162
Haines, Marriage of (1995) 33 CA4th 277, 39 CR2d 673: §§4.21, 10.33
Hall v Butte Home Health, Inc. (1997) 60 CA4th 308, 70 CR2d 246: §6.102
Hallmark Ins. Co. v Superior Court (1988) 201 CA3d 1014, 247 CR 638: §§15.40, 15.66
Hamilton v Board of Supervisors (1969) 269 CA2d 64, 75 CR 106: §4.87
Hamud v Hawthorne (1959) 52 C2d 78, 338 P2d 387: §10.41
Handy v Gordon (1967) 65 C2d 578, 55 CR 769: §§9.74-9.76, 9.80, 9.101
Hangarter v Provident Life & Acc. Ins. Co. (9th Cir 2004) 373 F3d 998: §§13.117, 13.122
Hannon v Western Title Ins. Co. (1989) 211 CA3d 1122, 260 CR 21: §§15.19, 15.37
Hanshaw v Long Valley Road Ass'n (2004) 116 CA4th 471, 11 CR3d 357: §§11.30, 11.77
Hanson v Prudential Ins. Co. (9th Cir 1985) 772 F2d 580: §13.112
Harbor Ins. Co. v Lewis (ED Pa 1983) 562 F Supp 800: §14.38
Harrah, Joseph A. (1958) 30 TC 1236: §9.21
Harrington v Department of Real Estate (1989) 214 CA3d 394, 263 CR 528: §2.3
Harris v Capital Growth Investors XIV (1991) 52 C3d 1142, 278 CR 614: §6.101
Harris v Rudin, Richman & Appel (1999) 74 CA4th 299, 87 CR2d 822: §3.20
Harrison v Welch (2004) 116 CA4th 1084, 11 CR3d 92: §§11.57, 11.77
Hartford Acc. & Indem. Co v IAC (1928) 93 CA 313, 269 P 733: §2.18
Hartman v Rizzuto (1954) 123 CA2d 186, 266 P2d 539: §§4.50, 4.66
Hartong v Partake, Inc. (1968) 266 CA2d 942, 72 CR 722: §6.73
Hartzheim v Valley Land & Cattle Co. (2007) 153 CA4th 383, 62 CR3d 815: §8.58
Harvey v The Landing Homeowners Ass'n (2008) 162 CA4th 809, 76 CR3d 41: §10.2
Hasekian v Krotz (1968) 268 CA2d 311, 74 CR 410: §2.5
Hasler v Howard (2004) 120 CA4th 1023, 16 CR3d 217: §2.158
Hawkins v State Bar (1979) 23 C3d 622, 153 CR 234: §1.11
Hays v Vanek (1989) 217 CA3d 271, 266 CR 856: §§11.57, 11.77
Heckert v MacDonald (1989) 208 CA3d 832, 256 CR 369: §2.158
Hedges v Carrigan (2004) 117 CA4th 578, 11 CR3d 787: §§2.85, 2.154, 6.18
Heffernan v Merrill Estate Co. (1946) 77 CA2d 106, 174 P2d 710: §2.59
Hellinger v Farmers Ins. Exch. (2001) 91 CA4th 1049, 111 CR2d 268: §13.93
Helm v Wilson (1888) 76 C 476, 18 P 604: §11.88
Henderson v Fisher (1965) 236 CA2d 468, 46 CR 173: §4.11
Henneberry v Henneberry (1958) 164 CA2d 125, 330 P2d 250: §10.71
Hennefer v Butcher (1986) 182 CA3d 492, 227 CR 318: §8.9
Henry v Associated Indem. Corp. (1990) 217 CA3d 1405, 266 CR 578: §13.121
Herdan v Hanson (1920) 182 C 538, 189 P 440: §2.184
Hergenroeder v Travelers Prop. & Cas. Co. (ED Cal 2008) 249 FRD 595: §13.117B
Herman v Mortensen (1945) 72 CA2d 413, 164 P2d 551: §10.75
Hernandez v City of Hanford (2007) 41 C4th 279, 59 CR3d 442: §4.86
Herrera v Department of Real Estate (2001) 88 CA4th 776, 106 CR2d 232: §§2.171, 2.173
Herring v Fisher (1952) 110 CA2d 322, 242 P2d 963: §2.106
Herzog v Capital Co. (1945) 27 C2d 349, 164 P2d 8: §§2.185, 6.30, 6.31A
Hickman v London Assur. Corp. (1920) 184 C 524, 195 P 45: §13.92
Hicks v Wilson (1925) 197 C 269, 240 P 289: §§2.42, 2.67
Hildebrand v Beck (1925) 196 C 141, 236 P 301: §§10.76, 15.27
Hill v Allan (1968) 259 CA2d 470, 66 CR 676: §11.66
Hill v Citizens Nat'l Trust & Sav. Bank (1937) 9 C2d 172, 69 P2d 853: §2.30
Hill v Donnelly (1941) 43 CA2d 47, 110 P2d 135: §10.73
Hill v Physicians & Surgeons Exch. (1990) 225 CA3d 1, 274 CR 702: §14.14A
Hill v Pinque (1922) 56 CA 245, 204 P 1097: §4.73
Hirshfield v Schwartz (2001) 91 CA4th 749, 110 CR2d 861: §11.57
Hoar v Tuley (1970) 12 CA3d 344, 90 CR 559: §§2.13, 2.94

Hobart v Hobart Estate Co. (1945) 26 C2d 412, 159 P2d 958: §6.73
Hobson v Hunt (1922) 59 CA 679, 211 P 242: §2.116
Hochstein v Romero (1990) 219 CA3d 447, 268 CR 202: §§12.2, 15.86-15.87, 15.91
Hocking v Title Ins. & Trust Co. (1951) 37 C2d 644, 234 P2d 625: §§4.50, 4.55, 11.10
Hodge v Hodge (1967) 257 CA2d 31, 64 CR 587: §10.60
Hoffman v State Farm Fire & Cas. Co. (1993) 16 CA4th 184, 19 CR2d 809: §§13.19, 13.22
Hogan v Midland Nat'l Ins. Co. (1970) 3 C3d 553, 91 CR 153: §§14.26, 14.54
Holiday Inns of Am. v Knight (1969) 70 C2d 327, 74 CR 722: §8.21
Holiday Inns of Am., Inc. v Knight (1969) 70 C2d 327, 74 CR 722: §8.33
Holland v McCarthy (1916) 173 C 597, 160 P 1069: §2.42
Holland v Morgan & Peacock Prop. Co. (1959) 168 CA2d 206, 335 P2d 769: §2.52
Holley v Crank (9th Cir 2004) 400 F3d 667: §2.15
Holley v Crank (9th Cir 2004) 386 F3d 1248: §2.15
Hollingsworth v Commercial Union Ins. Co. (1989) 208 CA3d 800, 256 CR 357: §14.71
Holloway v Thiele (1953) 116 CA2d 68, 253 P2d 131: §§2.69, 2.149
Home Ins. Co. v Landmark Ins. Co. (1988) 205 CA3d 1388, 253 CR 277: §13.80
Home Sav. v Continental Ins. Co. (2001) 87 CA4th 835, 104 CR2d 790: §§13.28-13.29, 14.21
Homestead Ins. Co. v American Empire Surplus Lines Ins. Co. (1996) 44 CA4th 1297, 52 CR2d 268: §§14.12-14.13
Hopkins v Fresno County Abstract Co. (1918) 36 CA 699, 173 P 106: §15.87
Horace Mann Ins. Co. v Barbara B. (1993) 4 C4th 1076, 17 CR2d 210: §14.54
Horn, Estate of (1951) 102 CA2d 635, 228 P2d 99: §6.88
Horning v Shilberg (2005) 130 CA4th 197, 29 CR3d 717: §2.96
Horowitz v Noble (1978) 79 CA3d 120, 144 CR 710: §§11.54-11.55
Horton v Kyburz (1959) 53 C2d 59, 346 P2d 399: §4.11
Hotaling v Hotaling (1924) 193 C 368, 224 P 455: §§10.72, 12.6
Hotel del Coronado Corp. v Foodservice Equip. Distribs. Ass'n (9th Cir 1986) 783 F2d 1323: §3.21
House of Prayer v Evangelical Assoc. for India (2003) 113 CA4th 48, 7 CR3d 24: §4.13
Houston v Williams (1921) 53 CA 267, 200 P 55: §2.58
Howell v State Farm Fire & Cas. Co. (1990) 218 CA3d 1446, 267 CR 708: §13.84
Hubbard v Brown (1990) 50 C3d 189, 266 CR 491: §11.43
Hudemann v Dodson (1932) 215 C 3, 7 P2d 997: §10.71
Hudson Props. Co. v Governing Bd. (1985) 168 CA3d 63, 213 CR 909: §§8.1, 9.53
Hughes v Grandy (1947) 78 CA2d 555, 177 P2d 939: §10.77
Hughes v Morrison (1984) 160 CA3d 103, 206 CR 321: §2.48
Hughes v Potomac Ins. Co. (1962) 199 CA2d 239, 18 CR 650: §§13.69, 13.73, 13.97
Huijers v DeMarrais (1992) 11 CA4th 676, 14 CR2d 232: §§2.32, 2.129
Hulsman v Freland (1928) 205 C 345, 270 P 948: §2.186
Hunter v Vernon (1948) 85 CA2d 525, 193 P2d 139: §2.120
Huttlinger v Far W. Enters. (1955) 131 CA2d 808, 281 P2d 554: §2.119

I

IDC Construction, LLC v Admiral Ins. Co. (SD Fla 2004) 339 F Supp 2d 1342
I. E. Assocs. v Safeco Title Ins. Co. (1985) 39 C3d 281, 216 CR 438: §15.86
In re _____ (*see* name of party)
Insurance Co. of N. Am. v National Am. Ins. Co. (1995) 37 CA4th 195, 43 CR2d 518: §14.63
Insurance Co. of N. Am. v United States Gypsum Co. (4th Cir 1989) 870 F2d 148: §13.81
InterMetal Mexicana v Insurance Co. of N. Am. (3d Cir 1989) 866 F2d 71: §13.81
International Clinical Labs. v Stevens (ED NY 1989) 710 F Supp 466: §§7.64-7.65
Irvin v Petitfils (1941) 44 CA2d 496, 112 P2d 688: §11.56
Isaac v A&B Loan Co. (1988) 201 CA3d 307, 247 CR 104: §3.26
Isaacson v G. D. Robertson & Co. (1948) 85 CA2d 71, 192 P2d 486: §4.86
Israel-Curley v California Fair Plan (2005) 126 CA4th 123, 24 CR3d 1: §13.93
Itek Corp. v Chicago Aerial Indus. (Del 1968) 248 A2d 625: §§3.20, 3.28
Ito v Schiller (1931) 213 C 632, 3 P2d 1: §11.59
Iusi v Chase (1959) 169 CA2d 83, 337 P2d 79: §§2.52, 2.93
Iusi v City Title Ins. Co. (1963) 213 CA2d 582, 28 CR 893: §15.22
Ivey v United Nat'l Indem. Co. (9th Cir 1958) 259 F2d 205: §13.107

J

J. Earl Oden (1971) 56 TC 569: §9.109
JEM Enters. v Washington Mut. Bank (2002) 99 CA4th 638, 121 CR2d 458: §13.26
JMR, Inc. v Hedderly (1968) 261 CA2d 144, 67 CR 742: §4.157
Jack Erickson & Assocs. v Hesselgesser (1996) 50 CA4th 182, 57 CR2d 591: §§9.72, 9.96
Jackson v Taylor (1969) 272 CA2d 1, 76 CR 891: §4.41
Jacobs v Freeman (1980) 104 CA3d 177, 163 CR 680: §§3.22, 3.40, 4.28, 6.21

Jacobus v Krambo Corp. (2000) 78 CA4th 1096, 93 CR2d 425: §7.66
Jacoves v United Merchandising Corp. (1992) 9 CA4th 88, 11 CR2d 468: §2.30
Jafari v EMC Ins. Cos. (review granted Dec. 12, 2007, S157924; superseded opinion at 155 CA4th 885, 66 CR3d 359: §14.20
Jang v State Farm Fire & Cas. Co. (2000) 80 CA4th 1291, 95 CR2d 917: §13.96
Janik v Rudy, Exelrod & Zieff (2004) 119 CA4th 930, 14 CR3d 751: §1.14
Jauman v McCusick (1913) 166 C 517, 137 P 254: §2.109
Jay v Dollarhide (1970) 3 CA3d 1001, 84 CR 538: §10.76
Jefferson Ins. Co. v Superior Court (1970) 3 C3d 398, 90 CR 608: §13.97
Jenkins v Tuneup Masters (1987) 190 CA3d 1, 235 CR 214: §§8.1, 8.20
Jennings v Karpe (1974) 36 CA3d 709, 111 CR 776: §2.171
Jewel Cos. v Pay Less Drug Stores NW. (9th Cir 1984) 741 F2d 1555: §3.22
Joanaco Projects, Inc. v Nixon & Tierney Constr. Co. (1967) 248 CA2d 821, 57 CR 48: §§9.83, 9.85
Joaquin, Marriage of (1987) 193 CA3d 1529, 239 CR 175: §8.22
Joerger v PG&E (1929) 207 C 8, 276 P 1017: §11.15
Johndrow v Thomas (1947) 31 C2d 202, 187 P2d 681: §15.89
Johnie Vaden Elrod (1986) 87 TC 1046: §§8.35, 8.39
Johnson v Cella (1953) 122 CA2d 72, 264 P2d 98: §4.64
Johnson v E-Z Ins. Brokerage, Inc. (2009) 175 CA4th 86, 95 CR3d 782: §§10.4, 12.10
Johnson v Ford Motor Co. (2005) 35 C4th 1191, 29 CR3d 401: §§13.118A, 13.118D
Johnson v Goldberg (1955) 130 CA2d 571, 279 P2d 131: §4.152
Johnson v Ocean Shore R.R. (1971) 16 CA3d 429, 94 CR 68: §§10.28, 11.71
Johnson v Siegel (2000) 84 CA4th 1087, 101 CR2d 412: §6.19
Jones v Crown Life Ins. Co. (1978) 86 CA3d 630, 150 CR 375: §13.107
Jones v Harmon (1959) 175 CA2d 869, 1 CR 192: §4.67
Jones v Sacramento Sav. & Loan Ass'n (1967) 248 CA2d 522, 56 CR 741: §9.76
Jones v Wells Fargo Bank (2003) 112 CA4th 1527, 5 CR3d 835: §9.6
Jones-Hamilton Co. v Kop-Coat, Inc. (ND Cal 1990) 750 F Supp 1022, aff'd in part on this issue and rev'd in part on other grounds sub nom Jones-Hamilton Co. v Beazer Mat'ls & Serv. (9th Cir 1992) 973 F2d 688: §7.67
Jones-Hamilton Co. v Kop-Coat, Inc. (ND Cal 1990) 750 F Supp 1022, rev'd in part on other grounds sub nom Jones-Hamilton Co. v Beazer Mat'ls & Serv. (9th Cir 1992) 973 F2d 688: §§7.61, 7.64
Jordan v Allstate Ins. Co. (2007) 148 CA4th 1062, 56 CR3d 312: §§13.86, 13.112, 13.117
Jordan v Allstate Ins. Co. (2004) 116 CA4th 1206, 11 CR3d 169: §§13.86-13.87
Jordan v Henck (1958) 166 CA2d 321, 333 P2d 117: §11.55
Jorgensen v Beach N' Bay Realty, Inc. (1981) 125 CA3d 155, 177 CR 882: §§2.124, 2.140
Joseph v Ager (1895) 108 C 517, 41 P 422: §11.66
Joseph A. Harrah (1958) 30 TC 1236: §9.21
Julian v Hartford Underwriters Ins. Co. (2005) 35 C4th 747, 27 CR3d 648: §§13.71, 13.74, 13.83, 13.86
Justice v Ackerman (1960) 183 CA2d 649, 6 CR 921: §2.100
Justy v Erro (1911) 16 CA 519, 117 P 575: §2.99

K

K F Dairies, Inc. & Affiliates v Fireman's Ins. Fund, Inc. (In re K F Dairies, Inc. & Affiliates) (9th Cir 2000) 224 F3d 922: §14.50
Kadner v Shields (1971) 20 CA3d 251, 97 CR 742: §4.3
Kahn v Chetcuti (2002) 101 CA4th 61, 123 CR2d 606: §6.19
Kalt, Estate of (1940) 16 C2d 807, 108 P2d 401: §10.24
Kalway v City of Berkeley (2007) 151 CA4th 827, 60 CR3d 477: §§1.83, 10.13
Kangarlou v Progressive Title Co. (2005) 128 CA4th 1174, 27 CR3d 754: §15.31
Kapner v Meadowlark Ranch Ass'n (2004) 116 CA4th 1182, 11 CR3d 138: §§11.15, 11.57, 11.77
Kapsimallis v Allstate Ins. Co. (2002) 104 CA4th 667, 128 CR2d 358: §13.94
Karoutas v HomeFed Bank (1991) 232 CA3d 767, 283 CR 809: §§6.30, 6.35
Kassir v Zahabi (2008) 164 CA4th 1352, 80 CR3d 1: §4.149
Katemis v Westerlind (1953) 120 CA2d 537, 261 P2d 553: §4.152
Katz v Department of Real Estate (1979) 96 CA3d 895, 158 CR 766: §§2.185, 4.120
Kay, Estate of (1947) 30 C2d 215, 181 P2d 1: §4.17
Kazi v State Farm Fire & Cas. Co. (2000) 24 C4th 871, 103 CR2d 1: §§11.43, 14.25
Keele v Clouser (1928) 92 CA 526, 268 P 682: §2.42
Keely v Price (1972) 27 CA3d 209, 103 CR 531: §2.121
Keith v Superior Court (1972) 26 CA3d 521, 103 CR 314: §11.70
Kelley v EPA (DC Cir 1994) 15 F3d 1100: §7.88
Kelley v Rouse (1961) 188 CA2d 92, 10 CR 235: §8.13
Kellogg v Garcia (2002) 102 CA4th 796, 125 CR2d 817: §11.56
Kelly v Smith (1933) 218 C 543, 24 P2d 471: §13.11
Keppelman v Heikes (1952) 111 CA2d 475, 245 P2d 54: §2.30
Key Tronic Corp. v U.S. (1994) 511 US 809, 128 L Ed 2d 797, 114 S Ct 1960: §7.19
Keys v Romley (1966) 64 C2d 396, 50 CR 273: §4.77

Keywell Corp. v Piper & Marbury, LLP (WD NY, Feb. 11, 1999, No. 96-CV-0660E) 1999 WL 66700, 1999 US Dist Lexis 1445: §4.45
King v Stanley (1948) 32 C2d 584, 197 P2d 321: §§2.95, 2.118, 4.50, 6.79, 8.9
King v Tilden Park Estates (1958) 156 CA2d 824, 320 P2d 109: §2.48
Kirby v Palos Verdes Escrow Co. (1986) 183 CA3d 57, 227 CR 785, disapproved on other grounds in Summit Fin. Holdings, Ltd. v Continental Lawyers Title Co. (2002) 27 C4th 705, 117 CR2d 541: §§15.18, 15.20, 15.23
Kirk Corp. v First Am. Title Co. (1990) 220 CA3d 785, 270 CR 24: §§15.7, 15.18
Kirkland v Risso (1979) 98 CA3d 971, 159 CR 798: §10.13
Kirschenmann v Commissioner (9th Cir 1973) 488 F2d 270: §9.28
Kish v Bay Counties Title Guar. Co. (1967) 254 CA2d 725, 62 CR 494: §§10.71, 15.27, 15.29
Kistler v Vasi (1969) 71 C2d 261, 78 CR 170: §4.41
Klamath Land & Cattle Co. v Roemer (1970) 12 CA3d 613, 91 CR 112: §§10.4, 12.22
Klemm v Superior Court (1977) 75 CA3d 893, 142 CR 509: §1.11
Knaugh v Baender (1927) 84 CA 142, 257 P 606: §10.55
Koch, Carl E. (1976) 67 TC 71, acq 1980 Cum Bull 1: §8.35
Kolodge v Boyd (2001) 88 CA4th 349, 105 CR2d 749: §9.8
Kopf v Milam (1963) 60 C2d 600, 35 CR 614: §§2.106, 2.108-2.109
Korea Supply Co. v Lockheed Martin Corp. (2003) 29 C4th 1134, 131 CR2d 29: §§2.122, 13.122
Korstad v Hoffman (1963) 221 CA2d Supp 805, 35 CR 61: §§2.99, 2.116
Kotlar v Hartford Fire Ins. Co. (2000) 83 CA4th 1116, 100 CR2d 246: §§14.32, 14.36-14.37
Kotrous v Goss-Jewett Co. (9th Cir 2008) 523 F3d 924: §7.17
Kovich v Paseo Del Mar Homeowners' Ass'n (1996) 41 CA4th 863, 48 CR2d 758: §6.61
Kowal v Day (1971) 20 CA3d 720, 98 CR 118: §§8.11, 8.13
Kraemer v Smith (1960) 179 CA2d 52, 3 CR 471: §2.115
Kraemer v Superior Oil Co. (1966) 240 CA2d 642, 49 CR 869: §11.78
Kransco v American Empire Surplus Lines Ins. Co. (2000) 23 C4th 390, 97 CR2d 151: §§13.112, 13.119
Kraus v Trinity Mgmt. Servs., Inc. (2000) 23 C4th 116, 96 CR2d 485: §13.122
Kritt v Athens Hills Dev. Co. (1952) 109 CA2d 642, 241 P2d 606: §2.78
Kroeker v Hurlbert (1940) 38 CA2d 261, 101 P2d 101: §2.134
Krone v Goff (1975) 53 CA3d 191, 127 CR 390: §13.26
Kropp v Sterling Sav. & Loan Ass'n (1970) 9 CA3d 1033, 88 CR 878: §10.75
Kruse v Miller (1956) 143 CA2d 656, 300 P2d 855: §2.163
Kunza v Gaskell (1979) 91 CA3d 201, 154 CR 101: §11.78
Kurtz v Calvo (1999) 75 CA4th 191, 89 CR2d 99: §9.9
Kytasty v Godwin (1980) 102 CA3d 762, 162 CR 556: §§10.2, 11.54, 11.106

L

L&B Real Estate v Housing Auth. of County of Los Angeles (2007) 149 CA4th 950, 57 CR3d 298: §10.76
L. Byron Culver & Assocs. v Jaoudi Indus. & Trading Corp. (1991) 1 CA4th 300, 1 CR2d 680: §2.129
La Mancha Dev. Corp. v Sheegog (1978) 78 CA3d 9, 144 CR 59: §15.20
La Sala v American Sav. & Loan Ass'n (1971) 5 C3d 864, 97 CR 849: §9.50
Ladas v California State Automobile Ass'n (1993) 19 CA4th 761, 23 CR2d 810: §6.5
Laing v Occidental Life Ins. Co. (1966) 244 CA2d 811, 53 CR 681: §13.107
Laks v Coast Fed. Sav. & Loan Ass'n (1976) 60 CA3d 885, 131 CR 836: §3.26
Lange v Schilling (2008) 163 CA4th 1412, 78 CR3d 356: §§2.153A, 6.19
Lange v TIG Ins. Co. (1998) 68 CA4th 1179, 81 CR2d 39: §3.26
Larkspur Isle Condominium Owners' Ass'n, Inc. v Farmers Ins. Group (1994) 31 CA4th 106, 37 CR2d 3: §§13.80, 13.82
Larwin-Southern California v JGB Inv. Co. (1979) 101 CA3d 626, 162 CR 52: §4.3
Lathrop v Gauger (1954) 127 CA2d 754, 274 P2d 730: §2.109
Lawler v Jacobs (2000) 83 CA4th 723, 100 CR2d 52: §§9.8, 9.48, 9.72, 9.99
Lawrence v Chicago Title Ins. Co. (1987) 192 CA3d 70, 237 CR 264: §§4.55, 6.80, 11.10, 11.75
Lawrence v Montgomery (1869) 37 C 183: §§12.6-12.7
Lawrence v Shutt (1969) 269 CA2d 749, 75 CR 533: §9.101
Lawrence Block Co. v Scholer (1958) 166 CA2d 608, 333 P2d 396: §§2.53, 2.115
Le Deit v Ehlert (1962) 205 CA2d 154, 22 CR 747: §11.69
Le Mesnager v Hamilton (1894) 101 C 532, 35 P 1054: §10.54
Lechusa Villas W. v California Coastal Comm'n (1997) 60 CA4th 218, 70 CR2d 399: §11.82
Lee v Escrow Consultants, Inc. (1989) 210 CA3d 915, 259 CR 117: §15.21
Lee v Helmco, Inc. (1962) 199 CA2d 820, 19 CR 413: §2.30
Lee v Lee (2009) 175 CA4th 1553, 97 CR3d 516: §10.76
Lee v O'Hara (1962) 57 C2d 476, 20 CR 617: §2.181
Lee v Title Ins. & Trust Co. (1968) 264 CA2d 160, 70 CR 378: §§15.16, 15.18, 15.21
Lehmann v Kamp (1969) 273 CA2d 701, 77 CR 910: §10.13
Lenny v Board of Supervisors (1974) 41 CA3d 902, 116 CR 500: §9.103
Leno v YMCA (1971) 17 CA3d 651, 95 CR 96: §2.26

Leonard v Fallas (1959) 51 C2d 649, 335 P2d 665: §§2.81, 2.112, 2.116
Leonard v Osburn (1915) 169 C 157, 146 P 530: §§10.42, 11.91
Lerner v Ward (1993) 13 CA4th 155, 16 CR2d 486: §4.153
Leslie v Federal Fin. Co (1939) 14 C2d 73, 92 P2d 906: §9.53
Levin v Knight (9th Cir 1986) 780 F2d 786: §3.25
Levitzky v Canning (1867) 33 C 299: §12.18
Lewis v Edmonds (1987) 190 CA3d 1101, 235 CR 835: §2.169
Lewis v Foppiano (1957) 150 CA2d 752, 310 P2d 658: §2.115
Lewis v Reed (1920) 48 CA 742, 192 P 335: §13.24
Lewis v State Bar of Cal. (1981) 28 C3d 683, 170 CR 634: §1.14
Lewis v Superior Court (1994) 30 CA4th 1850, 37 CR2d 63: §15.20
Lewis Operating Corp. v U.S. (CD Cal 2007) 533 F Supp 2d 1041: §7.25
Limsky v Scottish Union & Nat'l Ins. Co. (1924) 68 CA 688, 229 P 1017: §13.24
Lincoln Props. v Higgins (ED Cal 1993) 1993 US Dist Lexis 1251: §7.15
Lindsay v King (1956) 138 CA2d 333, 292 P2d 23: §4.64
Lingsch v Savage (1963) 213 CA2d 729, 29 CR 201: §§2.153, 2.178, 2.183-2.185, 4.49, 4.120, 6.31, 11.76, 12.22
Linthicum v Butterfield (2009) 175 CA4th 259, 95 CR3d 538: §11.57
Lipton v Johansen (1951) 105 CA2d 363, 233 P2d 648: §§2.109, 2.119
Litten v Warren (1936) 11 CA2d 635, 54 P2d 39: §10.23
Little v Stuyvesant Life Ins. Co. (1977) 67 CA3d 451, 136 CR 653: §13.116
Lockheed Corp. v Continental Ins. Co. (2005) 134 CA4th 187, 35 CR3d 799, disapproved on other grounds in State of California v Allstate Ins. Co. (2009) 45 C4th 1008, 90 CR3d 1: §14.49C
Locklin v City of Lafayette (1994) 7 C4th 327, 27 CR2d 613: §§4.77, 11.43
Loeb v Wilson (1967) 253 CA2d 383, 61 CR 377: §9.75
Logan v John Hancock Mut. Life Ins. Co. (1974) 41 CA3d 988, 116 CR 528: §13.107
Loken v Century 21-Award Props. (1995) 36 CA4th 263, 42 CR2d 683: §2.178
Long v Keller (1980) 104 CA3d 312, 163 CR 532: §§13.3, 13.8, 13.23
Lopez, Estate of (1992) 8 CA4th 317, 10 CR2d 67: §2.94
Los Angeles Mut. Ins. Co. v Cawog (1973) 30 CA3d 378, 106 CR 307: §13.110
Loughlin v Idora Realty Co. (1968) 259 CA2d 619, 66 CR 747: §2.133
Loughrin v Superior Court (1993) 15 CA4th 1188, 19 CR2d 161: §4.120
Louisiana v Braselman Corp. (ED La 1999) 78 F Supp 2d 543: §7.13
Louison v Yohanan (1981) 117 CA3d 258, 172 CR 602: §4.102
Love v Fire Ins. Exch. (1990) 221 CA3d 1136, 271 CR 246: §13.121
Love v White (1961) 56 C2d 192, 14 CR 442: §15.27
Low v Golden Eagle Ins. Co. (2002) 99 CA4th 109, 120 CR2d 827: §14.55
Lowe v Loyd (1949) 93 CA2d 684, 209 P2d 851: §§2.56, 2.63
Lucas v Hamm (1961) 56 Cal 2d 583, 15 CR 821: §1.14
Lyles v Perrin (1901) 134 C 417, 66 P 472: §12.13
Lyne v Bonner (1954) 129 CA2d 743, 277 P2d 941: §2.42
Lyon v Giannoni (1959) 168 CA2d 336, 335 P2d 690: §4.3

M

MacFadden v Walker (1971) 5 C3d 809, 97 CR 537: §9.16
MacKay v Darusmont (1941) 46 CA2d 21, 115 P2d 221: §10.39
MacKinnon v Truck Ins. Exch. (2003) 31 C4th 635, 3 CR3d 228: §14.17
Macedo v Bosio (2001) 86 CA4th 1044, 104 CR2d 1: §10.13
Machado v Southern Pac. Transp. Co. (1991) 233 CA3d 347, 284 CR 560: §§11.49, 11.71
Mackintosh v Agricultural Fire Ins. Co. (1907) 150 C 440, 89 P 102: §13.8
Macy Corp. v Ramey (Ohio CP 1957) 144 NE2d 698: §4.156
Madrid v Department of Real Estate (1984) 152 CA3d 454, 199 CR 520: §2.173
Maginnis v Hurlbutt (1917) 34 CA 504, 168 P 368: §11.27
Magna Dev. Co. v Reed (1964) 228 CA2d 230, 39 CR 284: §§9.74-9.75
Magnolia Square Homeowners Ass'n v Safeco Ins. Co. (1990) 221 CA3d 1049, 271 CR 1: §14.49
Main v Legnitto (1964) 230 CA2d 667, 41 CR 223: §11.73
Mains v City Title Ins. Co. (1949) 34 C2d 580, 212 P2d 873: §§12.7, 12.22
Major v Western Home Ins. Co. (2009) 169 CA4th 1197, 87 CR3d 556: §§13.105, 13.114-13.115, 13.117B
Maler v Superior Court (1990) 220 CA3d 1592, 270 CR 222: §13.123
Malerbi & Assocs. v Seivert (1961) 191 CA2d 760, 12 CR 852: §8.14
Mammoth Gold Dredging Co. v Forbes (1940) 39 CA2d 739, 104 P2d 131: §11.27
Manderville v PCG&S Group, Inc. (2007) 146 CA4th 1486, 55 CR3d 59: §§2.178, 6.73-6.74
Mangini v Aerojet-Gen. Corp. (1996) 12 C4th 1087, 51 CR2d 272: §7.20
Mangini v Aerojet-Gen. Corp. (1991) 230 CA3d 1125, 281 CR 827: §7.20
Mann v Montgomery (1907) 6 CA 646, 92 P 875: §12.7
Manufacturers Life Ins. Co. v Superior Court (Weil Ins. Agency) (1995) 10 C4th 257, 41 CR2d 220: §13.123

Marcus & Millichap Real Estate Inv. Brokerage Co. v Hock Inv. Co. (1998) 68 CA4th 83, 80 CR2d 147: §§4.150, 6.15, 6.18A
Mardan Corp. v C.G.C. Music, Ltd. (9th Cir 1986) 804 F2d 1454: §§7.61, 7.64
Mardan Corp. v C.G.C. Music, Ltd. (D Ariz 1984) 600 F Supp 1049: §§7.64-7.65, 7.67
Marin County Bd. of Realtors v Palsson (1976) 16 C3d 920, 130 CR 1: §2.118
Marin County Bd.of Realtors v Palsson (1976) 16 C3d 920, 130 CR 1: §2.41
Marina Point, Ltd. v Wolfson (1982) 30 C3d 721, 180 CR 496: §6.101
Markowitz v Fidelity Nat'l Title Co. (2006) 142 CA4th 508, 48 CR3d 217: §15.23
Marks v Rowley (1951) 102 CA2d 619, 228 P2d 29: §2.59
Marks v Walter G. McCarty Corp. (1949) 33 C2d 814, 205 P2d 1025: §§2.47-2.48
Maron v Howard (1968) 258 CA2d 473, 66 CR 70: §8.25
Maroon v Four Star Pizza, Inc. (In re Four Star Pizza, Inc.) (Bankr WD Pa 1992) 135 BR 498: §8.28
Marquez Knolls Prop. Owners Ass'n v Executive Risk Mgmt., Inc. (2007) 153 CA4th 228, 62 CR3d 510: §14.24
Marselis v Allstate Ins. Co. (2004) 121 CA4th 122, 16 CR3d 668: §13.95
Marsh v Lott (1908) 8 CA 384, 97 P 163: §8.11
Marshall v Marshall (1956) 140 CA2d 475, 295 P2d 131: §10.75
Martin v Culver Enterprises (1966) 239 CA2d 925, 49 CR 149: §2.107
Martin v World Sav. & Loan Ass'n (2001) 92 CA4th 803, 112 CR2d 225: §§13.21, 13.26
Marvin v Marvin (1976) 18 C3d 660, 134 CR 815: §6.89
Maryland Bank & Trust Co., U.S. v (D Md 1986) 632 F Supp 573: §§7.10-7.11, 7.88
Maryland Cas. Co. v Imperial Contracting Co. (1989) 212 CA3d 712, 260 CR 797: §14.63
Maryland Cas. Co. v Nationwide Ins. Co. (1998) 65 CA4th 21, 76 CR2d 113: §14.38
Maryland Cas. Co. v Reeder (1990) 221 CA3d 961, 270 CR 719: §§14.60, 14.63, 14.65
Masin v La Marche (1982) 136 CA3d 687, 186 CR 619: §11.64
Mason v Department of Real Estate (2002) 102 CA4th 1349, 126 CR2d 278: §2.170
Massei v Lettunich (1967) 248 CA2d 68, 56 CR 232: §4.77
Masterson v Sine (1968) 68 C2d 222, 65 CR 545: §§8.25, 11.15
Mattei v Hopper (1958) 51 C2d 119, 330 P2d 625: §§4.3, 6.21
Matthews v Hinton (1965) 234 CA2d 736, 44 CR 692: §9.85
Maxwell v Fire Ins. Exch. (1998) 60 CA4th 1446, 1450; 70 CR2d 866: §13.114
Mayhew v Burke (1929) 206 C 396, 274 P 517: §15.20
Maywood Mut. Water Co. No. 2 v City of Maywood (1972) 23 CA3d 266, 100 CR 174: §11.72
Mazuran v Stefanich (1928) 95 CA 327, 272 P 772: §1.19
McAlinden v Nelson (1953) 121 CA2d 136, 262 P2d 627: §2.108
McCarthy v Mutual Relief Ass'n (1889) 81 C 584, 22 P 933: §4.65
McCarty v Wilson (1920) 184 C 194, 193 P 578: §4.64
McConkey, Estate of (1939) 33 CA2d 554, 92 P2d 456: §4.16
McCorkle v State Farm Ins. Co. (1990) 221 CA3d 610, 270 CR 492: §§13.87, 13.107
McCormick v Marcy (1913) 165 C 386, 132 P 449: §§12.6, 12.9, 12.15, 12.17, 12.19
McCormick v Sentinel Life Ins. Co. (1984) 153 CA3d 1030, 200 CR 732: §13.112
McCormick v Travelers Ins. Co. (2001) 86 CA4th 404, 103 CR2d 258: §13.53
McCoy v Progressive W. Ins. Co. (2009) 171 CA4th 785, 90 CR3d 74: §13.120
McCoy v Progressive West Ins. Co. (2009) 171 CA4th 785, 90 CR3d 74: §13.120
McCulloch v M & C Beauty Colleges, Inc. (1987) 194 CA3d 1338, 240 CR 189: §§8.24, 8.58
McCullough v Olds (1895) 108 C 529, 41 P 420: §11.24
McGaughey v Fox (1979) 94 CA3d 645, 156 CR 593: §2.165
McGregor v Paul Revere Life Ins. Co. (9th Cir 2004) 369 F3d 1099: §13.115
McKeon v Millard (1874) 47 C 581: §11.29
McKinnon v Truck Ins. Exch. (2003) 31 C4th 635, 3 CR3d 228: §§13.45, 13.86, 13.141
McKnight v Dean (7th Cir 2001) 270 F3d 513: §2.142
McLain v Real Estate Bd. (1980) 444 US 232, 62 L Ed 2d 441, 100 S Ct 502: §2.118
McLaughlin v National Union Fire Ins. Co. (1994) 23 CA4th 1132, 29 CR2d 559: §14.25
McMillin Scripps North v Royal Ins. Co. (1993) 19 CA4th 1215, 23 CR2d 243: §13.112
McPike v Heaton (1900) 131 C 109, 63 P 179: §12.7
Meghrig v KFC W., Inc. (1996) 516 US 479, 134 L Ed 2d 121, 116 S Ct 1251: §§7.19-7.20
Mehdizadeh v Mincer (1996) 46 CA4th 1296, 54 CR2d 284: §§11.52, 11.77-11.78
Mejia v Community Hosp. (2002) 99 CA4th 1448, 122 CR2d 233: §2.30
Mejia v Reed (2003) 31 C4th 657, 3 CR3d 390: §10.13
Melendez v D & I Inv., Inc. (2005) 127 CA4th 1238, 26 CR3d 413: §11.11
Mendiondo v Greitman (1949) 93 CA2d 765, 209 P2d 817: §2.69
Mentry v Broadway Bank & Trust Co. (1912) 20 CA 388, 129 P 470: §10.69
Menzel v Salka (1960) 179 CA2d 612, 4 CR 78: §§2.126, 2.135, 2.140, 2.160-2.161
Mercury Ins. Co. v Ayala (2004) 116 CA4th 1198, 11 CR3d 158: §14.29
Merle v Meagher (1870) 1 CU 644: §10.53
Merlo v Standard Life & Acc. Ins. Co. (1976) 59 CA3d 5, 130 CR 416: §13.116
Merrifield v Edmonds (1983) 146 CA3d 336, 194 CR 104: §2.167

Merrill v Buck (1962) 58 C2d 552, 25 CR 456: §§2.159, 2.179
Mesnick v Caton (1986) 183 CA3d 1248, 228 CR 779: §11.78
Metropolitan Life Ins. Co. v State Bd. of Equalization (1982) 32 C3d 649, 186 CR 578: §13.81
Meyer v Holley (2003) 537 US 280, 154 L Ed 2d 753, 123 S Ct 824: §2.181
Mfrs. Life Ins. Co. v Superior Court (Weil Ins. Agency) (1995) 10 C4th 257, 41 CR2d 220: §13.122
Michel v Moore & Associates, Inc. (2007) 156 CA4th 756, 67 CR3d 797: §2.153
Michelson v Camp (1999) 72 CA4th 955, 85 CR2d 539: §9.48
Middlebrook-Anderson Co. v Southwest Sav. & Loan Ass'n (1971) 18 CA3d 1023, 96 CR 338: §§9.68, 9.80, 9.88
Middleton v Findla (1864) 25 C 76: §10.55
Migliore v Mid-Century Ins. Co. (2002) 97 CA4th 592, 118 CR2d 548: §13.93
Milazo v Gulf Ins. Co. (1990) 224 CA3d 1528, 274 CR 632: §14.34
Milian v DeLeon (1986) 181 CA3d 1185, 226 CR 831: §4.21
Miller v Citizens Sav. & Loan Ass'n (1967) 248 CA2d 655, 56 CR 844: §§9.83, 9.85
Miller v Jansen (1943) 21 C2d 473, 132 P2d 801: §10.73
Miller v Lerdo Land Co. (1921) 52 CA 662, 199 P 1073: §2.110
Miller v Western General Agency, Inc. (1996) 41 CA4th 1144, 49 CR2d 55: §§14.21-14.22, 14.29
Miller v Wood (1961) 188 CA2d 711, 10 CR 770: §2.184
Mills v Hellinger (1950) 100 CA2d 482, 224 P2d 34: §4.59
Millyard v Faus (1968) 268 CA2d 76, 73 CR 697: §11.31
Milmoe v Dixon (1950) 101 CA2d 257, 225 P2d 273: §6.31A
Milstein v Security Pac. Nat'l Bank (1972) 27 CA3d 482, 103 CR 16: §9.110
Mirabile, U.S. v (ED Pa 1985) 1985 US Dist Lexis 15411, 15 Envtl L Rep 20992: §7.88
Mission Nat'l Ins. Co. v Coachella Valley Water Dist. (1989) 210 CA3d 484, 258 CR 639: §§13.84, 13.86
Mitchell v Gould (1928) 90 CA 647, 266 P 565: §2.139
Mitchell v Johnston (1956) 140 CA2d Supp 982, 298 P2d 170: §2.47
Mitchell v Locurto (1947) 79 CA2d 507, 179 P2d 848: §2.42
Moallem v Coldwell Banker Commercial Group, Inc. (1994) 25 CA4th 1827, 31 CR2d 253: §4.153
Moe v Transamerica Title Ins. Co. (1971) 21 CA3d 289, 98 CR 547: §15.21
Monarch Tile, Inc. v City of Florence (11th Cir 2000) 212 F3d 1219: §7.88
Monarco v Lo Greco (1950) 35 C2d 621, 220 P2d 737: §3.14
Money Store Inv. Corp. v Southern Cal. Bank (2002) 98 CA4th 722, 120 CR2d 58: §§15.13, 15.18, 15.23, 15.59
Monsanto Co., U.S. v (4th Cir 1988) 858 F2d 160: §7.23
Monticello Ins. Co. v Essex Ins. Co. (2008) 162 CA4th 1376, 76 CR3d 848: §§14.38-14.39, 14.55
Montrose Chem. Corp. v Admiral Ins. Co. (1995) 10 C4th 645, 42 CR2d 324 (Montrose II): §§13.82, 14.2, 14.12, 14.17-14.18, 14.47-14.48, 14.53
Montrose Chem. Corp. v Superior Court (1993) 6 C4th 287, 24 CR2d 467 (Montrose I): §§14.53, 14.55
Montrose Chem. Corp., California v (9th Cir 1997) 104 F3d 1507: §7.20
Montrose Chemical Corp. v Admiral Ins. Co. (1995) 10 C4th 645, 42 CR2d 324, 913 P2d 878 (Montrose II): §14.49A
Moody v Osborne (1953) 120 CA2d 598, 261 P2d 783: §2.140
Moore v Smaw (1861) 17 C 199: §10.44
Moores v Walsh (1995) 38 CA4th 1046, 45 CR2d 389: §11.56
Moradi-Shalal v Fireman's Fund Ins. Co. (1988) 46 C3d 287, 250 CR 116: §§2.171, 13.123
Morehart v County of Santa Barbara (1994) 7 C4th 725, 29 CR2d 804: §§10.42, 11.14, 11.24
Morris v Employers Reinsurance Corp. (2000) 84 CA4th 1026, 101 CR2d 350: §§14.72, 14.75
Morse v County of San Luis Obispo (1967) 247 CA2d 600, 55 CR 710: §4.86
Mosee v Firemen's Fund Ins. Co. (1927) 87 CA 473, 262 P 436: §13.21
Moss v Minor Props. (1968) 262 CA2d 847, 69 CR 341: §15.12
Mott v Cline (1927) 200 C 434, 253 P 718: §8.25
Mt. Hawley Ins. Co. v Federal Sav. & Loan Ins. Co. (CD Cal 1987) 695 F Supp 469: §14.14A
Muktarian v Barmby (1965) 63 C2d 558, 47 CR 483: §11.112
Munger v Moore (1970) 11 CA3d 1, 89 CR 323: §10.13
Murphy v Allstate Ins. Co. (1978) 83 CA3d 38, 147 CR 565: §13.96
Murphy v Burch (2009) 46 C4th 157, 92 CR3d 381: §11.56
Murphy v Munson (1949) 95 CA2d 306, 212 P2d 603: §4.12
Murphy v Sheftel (1932) 121 CA 533, 9 P2d 568: §4.79
Murphy Slough Ass'n v Avila (1972) 27 CA3d 649, 104 CR 136: §11.72
Murray v State Farm Fire & Cas. Co. (1990) 219 CA3d 58, 268 CR 33: §§13.86, 13.141
Muzzy Ranch Co. v Solano County Airport Land Use Comm'n (2008) 164 CA4th 1, 78 CR3d 691: §1.79

N

NLRB v Bildisco & Bildisco (1984) 465 US 513, 79 L Ed 2d 482, 104 S Ct 1188: §8.28
Nahrstedt v Lakeside Village Condominium Ass'n (1994) 8 C4th 361, 33 CR2d 63: §10.2
Nash v Superior Court (1978) 86 CA3d 690, 150 CR 394, disapproved on other grounds in Malcolm v Superior Court (1981) 29 C3d 518, 174 CR 694: §4.152
National Ass'n of Realtors, People v (1981) 120 CA3d 459, 174 CR 728: §2.41

National Auto. & Cas. Ins. Co. v California Cas. Ins. Co. (1983) 139 CA3d 336, 188 CR 670: §14.37
Neal v Farmers Ins. Exchange (1978) 21 C3d 910, 148 CR 389: §13.118
Nece v Bennett (1963) 212 CA2d 494, 28 CR 117: §6.31
Neff v Ernst (1957) 48 C2d 628, 311 P2d 849: §11.30
Nelson v Mayer (1954) 122 CA2d 438, 265 P2d 52: §§2.58, 2.99, 2.101
Neufeld v Balboa Ins. Co. (2000) 84 CA4th 759, 101 CR2d 151: §13.93
Neville Chem. Co., California v (9th Cir 2004) 358 F3d 661: §7.22
New Hampshire Ins. Co. v Vieira (9th Cir 1991) 930 F2d 696: §14.27
New Jersey v New York (1998) 523 US 767, 140 L Ed 2d 993, 118 S Ct 1726: §11.86
New York v Shore Realty Corp. (2d Cir 1985) 759 F2d 1032: §§7.10, 7.12, 7.15
Newhouse v Upchurch (1971) 22 CA3d 204, 99 CR 436: §9.16
Newport Bldg. Corp. v City of Santa Ana (1962) 210 CA2d 771, 26 CR 797: §9.103
Nguyen v Tran (2007) 157 CA4th 1032, 68 CR3d 906: §2.154
Nichols v Boswell-Alliance Constr. Corp. (1960) 181 CA2d 584, 5 CR 546: §2.63
Nicoll v Rudnick (2008) 160 CA4th 550, 72 CR3d 879: §§10.2, 10.44
Niecko v Emro Mktg. Co. (ED Mich 1991) 769 F Supp 973: §§7.61, 7.64-7.65
Nikora v Mayer (2d Cir 1958) 257 F2d 246: §4.3
Ninety Nine Invs., Ltd. v Overseas Courier Serv. (Singapore) Private, Ltd. (2003) 113 CA4th 1118, 6 CR3d 891: §§4.152, 15.59
Nippert v Warneke (1900) 128 C 501, 61 P 96: §4.65
Nippon Credit Bank v 1333 N. Cal. Blvd. (2001) 86 CA4th 486, 103 CR2d 421: §9.8
Nishiyama v Safeco Title Ins. Co. (1978) 85 CA3d Supp 1, 149 CR 355: §§4.55, 4.92
Nizuk v Gorges (1960) 180 CA2d 699, 4 CR 565: §2.28
No Oil, Inc. v City of Los Angeles (1974) 13 C3d 68, 118 CR 34: §4.95
Noel v Dumont Builders (1960) 178 CA2d 691, 3 CR 220: §3.14
Norcal Mut. Ins. Co. v Newton (2000) 84 CA4th 64, 100 CR2d 683: §2.30
Nordahl v Department of Real Estate (1975) 48 CA3d 657, 121 CR 794: §2.169
Noronha v Stewart (1988) 199 CA3d 485, 245 CR 94: §11.56
Norris v San Mateo County Title Co. (1951) 37 C2d 269, 231 P2d 493: §2.70
North Am. Bldg. Maintenance, Inc. v Fireman's Fund Ins. Co. (2006) 137 CA4th 627, 40 CR3d 468: §14.47
Northrup Grumman Corp. v Factory Mut. Ins. Co. (9th Cir 2009) 563 F3d 777: §13.87
Northwestern Title Sec. Co. v Flack (1970) 6 CA3d 134, 85 CR 693: §13.88
Norton v Jackson (1855) 5 C 262, aff'd sub nom Jackson v Norton (1856) 6 C 187: §12.17

O

Ocean Shore R.R. v Spring Valley Water Co. (1933) 218 C 86, 21 P2d 588: §4.64
Ocean Shore R.R., People v (1948) 32 C2d 406, 196 P2d 570: §§11.62-11.63
Ocean Shore R.R. Co. v Doelger (1960) 179 CA2d 222, 3 CR 706: §11.62
O'Connell v Lampe (1929) 206 C 282, 274 P 336: §4.11
O'Connor v Boeing N. Am., Inc. (9th Cir 2002) 311 F3d 1139: §7.20
O'Connor v Village Green Owners Ass'n (1983) 33 C3d 790, 191 CR 320: §6.101
Oden, J. Earl (1971) 56 TC 569: §9.109
Oesterreich v Commissioner (9th Cir 1955) 226 F2d 798: §9.20
Ohanesian v Watson (1953) 118 CA2d 386, 257 P2d 1022: §2.129
Okun v Morton (1988) 203 CA3d 805, 250 CR 220: §3.21
Old Republic Ins. Co. v Superior Court (1998) 66 CA4th 128, 77 CR2d 642, overruled on other grounds in Vandenberg v Superior Court (1999) 21 C4th 815, 88 CR2d 366: §§13.75, 14.51, 14.59
Olsen v Spomer (1961) 192 CA2d 99, 13 CR 392: §2.93
Olson v Cornwell (1933) 134 CA 419, 25 P2d 879: §10.3
OneBeacon America Ins. Co. v Fireman's Fund Ins. Co. (2009) 175 CA4th 183, 95 CR3d 808: §14.53
Opsal v United Servs. Auto. Ass'n (1991) 2 CA4th 1197, 10 CR2d 352: §13.112
Orr v Byers (1988) 198 CA3d 666, 244 CR 13: §15.20
Ortega Rock Quarry v Golden Eagle Ins. Corp. (2006) 141 CA4th 969, 46 CR 3d 517: §14.68A
Osterberg v Osterberg (1945) 68 CA2d 254, 156 P2d 46: §10.73
Otis Elevator Co. v Toda Constr. (1994) 27 CA4th 559, 32 CR2d 404: §7.66
Ott v Home Sav. & Loan Ass'n (9th Cir 1958) 265 F2d 643: §4.157
Overgaard v Johnson (1977) 68 CA3d 821, 137 CR 412: §§2.155, 2.157, 2.163
Owens v Schneider (1938) 29 CA2d 593, 85 P2d 198: §2.184
Owens v Foundation for Ocean Research (1980) 107 CA3d 179, 165 CR 571, overruled on other grounds in Applied Equip. v Litton Saudi Arabia Ltd. (1994) 7 C4th 503, 28 CR2d 475: §2.50

P

PG&E v Crockett Land & Cattle Co. (1924) 70 CA 283, 233 P 370: §11.70
PG&E v G.W. Thomas Drayage & Rigging Co. (1968) 69 C2d 33, 69 CR 561: §11.15
PG&E v Minnette (1953) 115 CA2d 698, 252 P2d 642: §11.48
PMC, Inc. v Sherwin-Williams Co. (7th Cir 1998) 151 F3d 610: §7.35

PPG Indus., Inc. v Transamerica Ins. Co. (1999) 20 C4th 310, 84 CR2d 455: §13.117
Pacific Coast Eng'g Co. v St. Paul Fire & Marine Ins. Co. (1970) 9 CA3d 270, 88 CR 122: §§13.55, 13.59
Pacific Employers Ins. Co. v Superior Court (1990) 221 CA3d 1348, 270 CR 779: §§14.12-14.13
Pacific Gas & Elec. Co. v Minnette (1953) 115 CA2d 698, 252 P 2d 642: §11.11
Pacific Heating & Ventilating Co. v Williamsburg City Fire Ins. Co. (1910) 158 C 367, 111 P 4: §13.84
Pacific Hide & Fur Depot, Inc., U.S. v (D Idaho 1989) 716 F Supp 1341: §§7.23, 7.25
Pacific Indem. Co. v Universal Underwriters Ins. Co. (1965) 232 CA2d 541, 43 CR 26: §14.17
Pacific Preferred Props. v Moss (1999) 71 CA4th 1456, 84 CR2d 500: §2.158
Pacific S.W. Dev. Corp. v Western Pac. R.R. (1956) 47 C2d 62, 301 P2d 825: §§2.48, 2.51, 9.53
Packer v Bird (1886) 71 C 134, 11 P 873: §11.84
Padgett v Phariss (1997) 54 CA4th 1270, 63 CR2d 373: §2.127
Padilla Constr. Co., Inc. v Transportation Ins. Co. (2007) 150 CA4th 984, 58 CR3d 807: §§14.53-14.54
Pagano v Krohn (1997) 60 CA4th 1, 70 CR2d 1: §§2.127, 6.32-6.32A, 6.73
Page v Principe (1963) 220 CA2d 151, 33 CR 836: §2.94
Palacin v Allstate Ins. Co. (2004) 119 CA4th 855, 14 CR3d 731: §13.37
Palo Alto Town & Country Village, Inc. v BBTC Co. (1974) 11 C3d 494, 113 CR 705: §§6.5, 8.20
Palos Verdes Corp. v Housing Auth. (1962) 202 CA2d 827, 21 CR 225: §§4.50, 12.4
Palub v Hartford Underwriters Ins. Co. (2001) 92 CA4th 645, 112 CR2d 270: §13.86
Palvutzian v Terkanian (1920) 47 CA 47, 190 P 503: §11.55
Panagotacos v Bank of America (1998) 60 CA4th 851, 70 CR2d 595: §6.5
Pardee Constr. Co. v Insurance Co. of the W. (2000) 77 CA4th 1340, 92 CR2d 443: §§13.23, 14.44
Park Redlands Covenant Control Comm. v Simon (1986) 181 CA3d 87, 226 CR 199: §6.103
Park Terrace Ltd. v Teasdale (2002) 100 CA4th 802, 122 CR2d 797: §2.9
Parsons v Bristol Dev. Co. (1965) 62 C2d 861, 44 CR 767: §11.49
Parsons v Smilie (1893) 97 C 647, 32 P 702: §10.50
Pasadena v California-Michigan (1941) 17 C2d 576, 110 P2d 983: §11.52
Pascal v Cotton (1962) 205 CA2d 597, 23 CR 357: §2.61
Patel v Liebermensch (2008) 45 C4th 344, 86 CR3d 366: §§4.4, 6.5, 8.9
Patillo v Norris (1976) 65 CA3d 209, 135 CR 210: §6.89
Patrick v Maryland Cas. Co. (1990) 217 CA3d 1566, 267 CR 24: §13.117
Patterson v Marchese (1960) 196 NYS2d 903: §4.83
Paul v Schoellkopf (2005) 128 CA4th 147, 26 CR3d 766: §15.31
Paul Harris Stores, Inc. v Mabel L. Salter Realty Trust (In re Paul Harris Stores, Inc.) (Bankr SD Ind 1992) 148 BR 307: §8.28
Paul Trans Dang, TC Memo 1999-233: §9.59
Paulsen v Leadbetter (1968) 267 CA2d 148, 72 CR 819: §2.47
Payne v White House Props., Inc. (1980) 112 CA3d 465, 169 CR 373: §2.18
Peak-Las Positas Partners v Bollag (2009) 172 CA4th 101, 90 CR3d 775: §§4.3, 4.149, 6.21, 15.59, 15.97
Pecarovich v Allstate Ins. Co. (9th Cir 2002) 309 F3d 652: §13.53
Pecarovich v Allstate Ins. Co. (CD Cal 2003) 272 F Supp 2d 981: §13.53
Pellandini v Valadao (2003) 113 CA4th 1315, 7 CR3d 413: §8.58
Pellissier v Title Guar. & Trust Co. (1929) 208 C 172, 280 P 947: §10.71
Penasquitos, Inc. v Holladay (1972) 27 CA3d 356, 103 CR 717: §§4.23, 8.32
Penn-America Ins. Co. v Mike's Tailoring (2005) 125 CA4th 884, 22 CR3d 918: §13.87
Pension Trust Fund v Federal Ins. Co. (9th Cir 2002) 307 F3d 944: §14.14
People v _____ (*see* name of defendant)
Pepitone v Russo (1976) 64 CA3d 685, 134 CR 709: §§2.144, 2.157
Pepper v Underwood (1975) 48 CA3d 698, 122 CR 343, disapproved on other grounds in Stout v Turney (1978) 22 C3d 718, 150 CR 637: §§2.143, 2.157
Pepperell v Scottsdale Ins. Co. (1998) 62 CA4th 1045, 73 CR2d 164: §§14.20, 14.49
Perry v Robertson (1988) 201 CA3d 333, 247 CR 74: §2.159
Perry v Wallner (1962) 206 CA2d 218, 23 CR 352: §6.106B
Peterson v Hartell (1985) 40 C3d 102, 219 CR 170: §9.16
Peterson v Ryan (1951) 108 CA2d 41, 238 P2d 117: §2.30
Pfeiffer v General Ins. Corp. (ND Cal 1960) 185 F Supp 605: §13.69
Phelps, In re (2001) 93 CA4th 451, 113 CR2d 217: §6.107
Phiffer v Proud Parrot Motor Hotel, Inc. (9th Cir 1980) 648 F2d 548: §6.99
Philip Morris USA v Williams (2007) 549 US 346, 166 L Ed 2d 940, 127 SCt 1057: §13.118A
Phillippe v Shapell Indus. (1987) 43 C3d 1247, 241 CR 22: §§2.43, 2.48, 2.50-2.51
Philmar Mid-Atlantic, Inc. v York St. Assocs II. (Pa Super 1989) 566 A2d 1253: §3.30
Phoenix Ins. Co. v Sukut Constr. Co. (1982) 136 CA3d 673, 186 CR 513: §14.14A
Phoenix Mut. Life Ins. Co. v Shady Grove Plaza Ltd. Partnership (D Md 1990) 734 F Supp 1181, aff'd without published opinion (4th Cir 1991) 937 F2d 603: §3.30
Piazzini v Jessup (1957) 153 CA2d 58, 314 P2d 196: §4.59
Pieper, Estate of (1964) 224 CA2d 670, 37 CR 46: §10.72
Pinal Creek Group v Newmont Mining Corp. (9th Cir 1997) 118 F3d 1298: §7.17

Pines of La Jolla Homeowners Ass'n v Industrial Indem. (1992) 5 CA4th 714, 7 CR2d 53: §13.82
Pittman v Canham (1992) 2 CA4th 556, 3 CR2d 340: §4.152
Planned Parenthood, Inc. v American Coalition of Life Activists (9th Cir 2005) 422 F3d 949: §13.118B
Plastino v Eureka Fed. Sav. & Loan Ass'n (In re Sunset Bay Assocs.) (9th Cir 1991) 944 F2d 1503: §9.88
Plaza Freeway Ltd. Partnership v First Mountain Bank (2000) 81 CA4th 616, 96 CR2d 865: §4.73
Podd v Anderson (1963) 215 CA2d 660, 30 CR 345: §§10.35, 10.42, 10.73
Polinsky v Vaughan (1968) 268 CA2d 183, 73 CR 764: §8.11
Pollard v Saxe & Yolles Dev. Co. (1974) 12 C3d 374, 115 CR 648: §§6.9, 6.30, 12.1
Pope v Mississippi Real Estate Comm'n (5th Cir 1989) 872 F2d 127: §2.41
Port Auth. of New York & New Jersey v Affiliated FM Ins. Co. (3rd Cir 2002) 311 F3d 226: §13.139
Porter, Estate of (1903) 138 C 618, 72 P 173: §§10.13, 12.5
Powerine Oil Co., Inc. v Superior Court (2005) 37 C4th 377, 33 CR3d 562: §§13.49, 14.25A
Powers v Fox (1979) 96 CA3d 440, 158 CR 92: §2.165
Prather v Vasquez (1958) 162 CA2d 198, 327 P2d 963: §§2.106, 8.13
Pray v Anthony (1929) 96 CA 772, 274 P 1024: §2.46
Preach v Monter Rainbow (1993) 12 CA4th 1441, 16 CR2d 320: §§2.5, 2.94
Preciado v Wilde (2006) 139 CA4th 321, 42 CR3d 792: §11.77
Preis v American Indem. Co. (1990) 220 CA3d 752, 269 CR 617: §§2.30, 14.41
Presley Homes, Inc. v American States Ins. Co. (2001) 90 CA4th 571, 108 CR2d 686: §§14.38-14.39
Price v DeReyes (1911) 161 C 484, 119 P 893: §11.78
Price, U.S. v (D NJ 1983) 577 F Supp 1103: §7.15
Prieto v State Farm Fire & Cas. Co. (1990) 225 CA3d 1188, 275 CR 362: §13.96
Prieto, Estate of (1966) 243 CA2d 79, 52 CR 80: §2.94
Pritchard v Kimball (1923) 190 C 757, 214 P 863: §8.25
Professional Equities, Inc. (1987) 89 TC 165: §§9.29, 9.60
Propst, Estate of (1990) 50 C3d 448, 268 CR 114: §6.87
Proulx v Sacramento Valley Land Co. (1912) 19 CA 529, 126 P 509: §2.46
Prouty v Gores Technol. Group (2004) 121 CA4th 1225, 18 CR3d 178: §4.163
Providence Washington Ins. Co. v Valley Forge Ins. Co. (1996) 42 CA4th 1194, 50 CR2d 192: §14.33
Prudential-LMI Commercial Ins. v Superior Court (1990) 51 C3d 674, 274 CR 387: §§13.80, 13.82, 13.94-13.95
Prudential-LMI Commercial Ins. Co. v Superior Court (1990) 51 C3d 674, 274 CR 387, 798 P2d 1230: §§13.93, 14.49B
Prudential-LMI Commercial Ins. Co. v Reliance Ins. Co. (1994) 22 CA4th 1508, 27 CR2d 841: §14.60
Pruyn v Agricultural Ins. Co. (1995) 36 CA4th 500, 42 CR2d 295: §13.90
Puccetti v Girola (1942) 20 C2d 574, 128 P2d 13: §10.20

Q

Quality Wash Group V, Ltd. v Hallak (1996) 50 CA4th 1687, 58 CR2d 592: §4.111
Quan v Truck Ins. Exch. (1998) 67 CA4th 583, 79 CR2d 134: §14.19
Quan Shew Yung v Woods (1963) 218 CA2d 506, 32 CR 453: §3.26
Quelimane Co. v Stewart Title Guar. Co. (1998) 19 C4th 26, 77 CR2d 709: §11.10

R

R&R Sails, Inc. v Insurance Co. of the State of Pennsylvania (SD Cal 2009) 610 F Supp 2d 1222: §§13.60, 13.120, 13.122
R.J. Kuhl Corp. v Sullivan (1993) 13 CA4th 1589, 17 CR2d 425: §§2.98, 2.102
RC Royal Dev't and Realty Corp. v Standard Pac. Corp.: §2.110
Racine & Laramie, Ltd. v Department of Parks & Recreation (1992) 11 CA4th 1026, 14 CR2d 335: §3.28
Rader Co. v Stone (1986) 178 CA3d 10, 223 CR 806: §§2.47-2.48
Radunich v Basso (1965) 235 CA2d 826, 45 CR 824: §§9.77, 9.85
Rafeiro v American Employers' Ins. Co. (1970) 5 CA3d 799, 85 CR 701: §§14.64-14.65
Raglan v Johnston Rock Co. (1942) 50 CA2d 705, 123 P2d 883: §11.82
Rakestraw v Rodriques (1972) 8 C3d 67, 104 CR 57: §2.29
Raley v California Tahoe Regional Planning Agency (1977) 68 CA3d 965, 137 CR 699: §4.86
Ramsdell v Krehmke (1928) 95 CA 195, 272 P 333: §2.106
Rattray v Scudder (1946) 28 C2d 214, 169 P2d 371: §§2.127, 2.140
Ray v Valley Forge Ins. Co. (1999) 77 CA4th 1039, 92 CR2d 473: §§14.21, 14.71
Ray Thomas Enters. v Fox (1982) 128 CA3d 361, 180 CR 253: §9.75
Real Estate Analytics, LLC v Vallas (2008) 160 CA4th 463, 72 CR3d 835: §4.149
Realmuto v Gagnard (2003) 110 CA4th 193, 1 CR3d 569: §§6.21, 6.34-6.36
Realty Corp. of Am. v Burton (1958) 162 CA2d 44, 327 P2d 948: §§2.53, 2.95
Realty Multi-List, Inc., U.S. v (5th Cir 1980) 629 F2d 1351: §2.41
Realty Projects, Inc. v Smith (1973) 32 CA3d 204, 108 CR 71: §§2.8, 2.125
Red Mountain LLC v Fallbrook Pub. Util. Dist. (2006) 143 CA4th 333, 48 CR3d 875: §§10.42, 11.15
Redevelopment Agency v Salvation Army (2002) 103 CA4th 755, 127 CR2d 30: §7.15
Redevelopment Agency v San Diego Gas & Elec. Co. (2003) 111 CA4th 912, 4 CR3d 317: §7.15
Reed v King (1983) 145 CA3d 261, 193 CR 130: §§6.31, 6.65

Reese v Borghi (1963) 216 CA2d 324, 30 CR 868: §11.56
Reese v Wong (2001) 93 CA4th 51, 112 CR2d 669: §4.145
Regan Roofing Co. v Superior Court (1994) 24 CA4th 425, 29 CR2d 413: §14.53
Reichardt v Hoffman (1997) 52 CA4th 754, 60 CR2d 770: §§11.43, 11.61-11.62
Reilly Tar & Chem. Co., U.S. v (D Minn 1985) 606 F Supp 412: §7.15
Renaissance Realty, Inc. v Soriano (1981) 120 CA3d Supp 13, 174 CR 837: §2.123
Reprosystem, B.V. v SCM Corp. (2d Cir 1984) 727 F2d 257: §§3.19, 3.23, 3.26
Rhoades v Savage (1963) 219 CA2d 294, 32 CR 885: §2.171
Rianda v San Benito Title Guar. Co. (1950) 35 C2d 170, 217 P2d 25: §15.18
Rice v Taylor (1934) 220 C 629, 32 P2d 381: §§12.2, 15.20
Richard v Baker (1956) 141 CA2d 857, 297 P2d 674: §2.184
Richards Realty Co. v Real Estate Comm'r (1956) 144 CA2d 357, 300 P2d 893: §2.145
Richmond Ramblers Motorcycle Club v Western Title Guar. Co. (1975) 47 CA3d 747, 121 CR 308: §11.77
Rickless v Temple (1970) 4 CA3d 869, 84 CR 828: §10.13
Ridgley v Topa Thrift & Loan Ass'n (1998) 17 C4th 970, 73 CR2d 378: §9.30
Ridgway v Chase (1954) 122 CA2d 840, 265 P2d 603: §2.115
Riley v Mid-Century Ins. Exch. (1981) 118 CA3d 195, 173 CR 257: §13.15
Rivadell, Inc. v Razo (1963) 215 CA2d 614, 30 CR 622: §4.157
Riverside Fence Co. v Novak (1969) 273 CA2d 656, 78 CR 536: §§8.5, 8.20-8.21, 8.23, 8.57
Roberts v Adams (1958) 164 CA2d 312, 300 P2d 900: §8.14
Roberts v Assurance Co. of Am. (2008) 163 CA4th 1398, 78 CR3d 361: §§13.76, 13.83, 13.87
Roberts v Lebrain (1952) 113 CA2d 712, 248 P2d 810: §11.15
Roberts v Lomanto (2003) 112 CA4th 1553, 5 CR3d 866: §2.177
Robinson v Elliot (9th Cir 1958) 262 F2d 383: §9.20
Robinson v Grossman (1997) 57 CA4th 634, 67 CR2d 380: §2.150
Robinson v Murphy (1979) 96 CA3d 763, 158 CR 246: §§2.6, 2.165
Robson v O'Toole (1919) 45 CA 63, 187 P 110: §4.41
Rodes v Shannon (1963) 222 CA2d 721, 35 CR 339: §2.160
Rodriguez v Barnett (1959) 52 C2d 154, 338 P2d 907: §§4.3, 4.92
Rodriguez v Department of Real Estate (1996) 51 CA4th 1289, 59 CR2d 652: §2.170
Roemer v Pappas (1988) 203 CA3d 201, 249 CR 743: §11.56
Roger H. Proulx & Co. v Crest-Liners, Inc. (2002) 98 CA4th 182, 119 CR2d 442: §§14.41, 14.63
Rogers v Grua (1963) 215 CA2d 1, 30 CR 39: §2.45
Rogers v McCartney (1906) 3 CA 34, 84 P 215: §§10.42, 11.91
Roland v Hubenka (1970) 12 CA3d 215, 90 CR 490: §4.59
Rollins v Stokes (1981) 123 CA3d 701, 176 CR 835: §8.23
Rolon v Kulwitzky (1984) 153 CA3d 289, 200 CR 217: §6.106
Romo v Stewart Title (1995) 35 CA4th 1609, 42 CR2d 414: §15.21
Root v American Equity Specialty Ins. Co. (2005) 130 CA4th 926, 30 CR3d 631: §14.15
Rooz v Kimmel (1997) 55 CA4th 573, 64 CR2d 177: §§15.24, 15.31
Rose v Hunter (1957) 155 CA2d 319, 317 P2d 1027: §§2.99-2.100
Rosen v State Farm Gen. Ins. Co. (2003) 30 C4th 1070, 135 CR2d 361: §13.86
Rosenaur v Pacelli (1959) 174 CA2d 673, 345 P2d 102: §8.32
Rosenblum v Safeco Ins. Co. (2005) 126 CA4th 847, 24 CR3d 427: §13.93
Rosenthal v Great W. Fin. Sec. Corp. (1996) 14 C4th 394, 58 CR2d 875: §4.150
Roth v Garcia Marquez (9th Cir 1991) 942 F2d 617: §§3.19, 3.21
Roth v Malson (1998) 67 CA4th 552, 79 CR2d 226: §6.5
Rothstein v Janss Inv. Corp. (1941) 45 CA2d 64, 113 P2d 465: §2.184
Royal Indem. Co. v IAC (1930) 104 CA 290, 285 P 912: §2.18
Royal Ins. Co. v Sisters of Presentation (9th Cir 1970) 430 F2d 759: §§13.16-13.17
Rubin v Los Angeles Fed. Sav. & Loan Ass'n (1984) 159 CA3d 292, 205 CR 455: §9.53
Rule, Estate of (1944) 25 C2d 1, 152 P2d 1003, disapproved on other grounds in Parsons v Bristol Dev. Co. (1965) 62 C2d 861, 44 CR 767: §2.47
Rupp v Kahn (1966) 246 CA2d 188, 55 CR 108: §§4.22, 6.87
Russell v Ramm (1927) 200 C 348, 254 P 532: §2.106
Russell v Williams (1962) 58 C2d 487, 24 CR 859: §13.23
Rustigian v Phelps (1923) 190 C 608, 213 P 957: §4.64
Ruth v Lytton Sav. & Loan Ass'n (1968) 266 CA2d 831, 72 CR 521: §§9.76-9.77
Rylander v Karpe (1976) 60 CA3d 317, 131 CR 415: §§2.131, 2.135
Rylee v Defini (1955) 134 CA2d Supp 877, 285 P2d 115: §2.107

S

SDC/Pullman Partners v Tolo Inc. (1997) 60 CA4th 37, 70 CR2d 62: §7.21
SEMX Corp. v Federal Ins. Co. (SD Cal 2005) 398 F Supp 2d 1103: §13.93
Sabella v Wisler (1963) 59 C2d 21, 27 CR 689: §13.81

Sackett v Los Angeles City Sch. Dist. (1931) 118 CA 254, 5 P2d 23: §4.66
Sacramento Sav. & Loan Ass'n v Superior Court (1982) 137 CA3d 142, 186 CR 823: §9.45
Safeco Ins. Co. v Fireman's Fund Ins. Co. (2007) 148 CA4th 620, 55 CR3d 844: §§14.47, 14.49D, 14.53
Safeco Ins. Co. v Guyton (9th Cir 1982) 692 F2d 551: §13.112
Safeco Ins. Co. v Robert S. (2001) 26 C4th 758, 110 CR2d 844: §13.86
Safeco Ins. Co. v Sharma (1984) 160 CA3d 1060, 207 CR 104: §13.97
Safeco Surplus Lines Co. v Employers' Reinsurance Corp. (1992) 11 CA4th 1403, 15 CR2d 58: §14.14A
Sain v Silvestre (1978) 78 CA3d 461, 144 CR 478, disapproved on other grounds in Reynolds Metals Co. v Alperson (1979) 25 C3d 124, 158 CR 1: §4.66
Salahutdin v Valley of Cal., Inc. (1994) 24 CA4th 555, 29 CR2d 463: §§2.127, 2.150, 2.155, 6.7
Salmon v Vallejo (1871) 41 C 481: §§12.6-12.8
Salveter v Salveter (1929) 206 C 657, 275 P 801: §10.39
San Diego Constr. Co. v Mannix (1917) 175 C 548, 166 P 325: §9.105
San Diego Hospice v County of San Diego (1995) 31 CA4th 1048, 37 CR2d 501: §6.30
San Diego Housing Comm'n v Industrial Indem. Co. (1998) 68 CA4th 526, 80 CR2d 393: §13.112
San Diego Watercrafts, Inc. v Wells Fargo Bank, N.A. (2002) 102 CA4th 308, 125 CR2d 499: §8.58
San Francisco Indus. Park, In re (ND Cal 1969) 307 F Supp 271: §9.20
San Jose Crane & Rigging, Inc. v Lexington Ins. Co. (1991) 227 CA3d 1314, 278 CR 301: §13.95
San Rafael Ranch Co. v Ralph Rogers Co. (1908) 154 C 76, 96 P 1092: §11.47
Sanders v Magill (1937) 9 C2d 145, 70 P2d 159: §4.42
Sanfran Co. v Rees Blow Pipe Mfg. Co. (1959) 168 CA2d 191, 335 P2d 995: §6.72
Santa Margarita Area Residents Together v San Luis Obispo County Bd. of Supervisors (2000) 84 CA4th 221, 100 CR2d 740: §4.86
Santisas v Goodin (1998) 17 C4th 599, 71 CR2d 830: §4.153
Santos v Wing (1961) 197 CA2d 678, 17 CR 457: §§2.146, 2.147A
Sapiro v Encompass Ins. (ND Cal 2004) 221 FRD 513: §§13.80, 13.84, 13.86-13.87, 13.141
Saporta v Barbagelata (1963) 220 CA2d 463, 33 CR 661: §§2.178, 2.183
Sarten v Pomatto (1961) 192 CA2d 288, 13 CR 588: §2.42
Saterstrom v Glick Bros. Sash Co. (1931) 118 CA 379, 5 P2d 21: §§10.42, 11.14
Saunders v Schmaelzle (1874) 49 C 59: §11.102
Saunders v Taylor (1996) 42 CA4th 1538, 50 CR2d 395: §6.35
Savage v Mayer (1949) 33 C2d 548, 203 P2d 9: §§2.69, 2.131, 2.135, 2.160
Save El Toro Ass'n v Days (1977) 74 CA3d 64, 141 CR 282: §1.76
Scarbery v Bill Patch Land & Water Co. (1960) 184 CA2d 87, 7 CR 408: §8.39
Schade v Stewart (1928) 205 C 658, 272 P 567: §§10.25, 10.76
Schaffter v Creative Capital Leasing Group, LLC (2008) 166 CA4th 745, 83 CR3d 19: §§2.63, 2.89
Schantz v Ellsworth (1971) 19 CA3d 289, 96 CR 783: §2.94
Scheerer v Cuddy (1890) 85 C 270, 24 P 713: §§11.11, 12.2
Scherz v S.C. Ins. Co. (CD Cal 2000) 112 F Supp 2d 1000: §13.53
Schmidt v Beckelman (1960) 187 CA2d 462, 9 CR 736: §8.33
Schneider v Ampliflo Corp. (1983) 148 CA3d 637, 196 CR 172: §9.75
Schoenberg v Romike Props. (1967) 251 CA2d 154, 59 CR 359: §2.142
Schofield v Bany (1959) 175 CA2d 534, 346 P2d 891: §11.68
Schoolcraft v Ross (1978) 81 CA3d 75, 146 CR 57: §13.26
Schwartz v Dibblee (1921) 51 CA 451, 197 P 125: §§11.93, 11.103
Scott v Continental Ins. Co. (1996) 44 CA4th 24, 51 CR2d 566: §§13.86, 13.141
Scottsdale Ins. Co. v MV Transp. (2005) 36 C4th 643, 31 CR3d 147: §§14.53, 14.55-14.56
Scottsdale Ins. Co., 36 C4th 643 at 657: §14.53
Scruby v Vintage Grapevine, Inc. (1995) 37 CA4th 697, 43 CR2d 810: §11.43
Seaman's Direct Buying Serv. v Standard Oil Co. (1984) 36 C3d 752, 206 CR 354, overruled on other grounds in Della Penna v Toyota Motor Sales, U.S.A., Inc. (1995) 11 C4th 376, 45 CR2d 436: §3.18
Seaman's Direct Buying Serv. v Standard Oil Co. (1984) 36 C3d 752, 206 CR 354, overruled on other grounds in Freeman & Mills v Belcher Oil Co. (1995) 11 C4th 85, 44 CR2d 420: §3.25
Seck v Foulks (1972) 25 CA3d 556, 102 CR 170: §§2.45, 2.54, 2.76, 2.95, 2.97, 2.110
Security Co. v Rice (1932) 215 C 263, 9 P2d 817: §10.44
Security Pac. Nat'l Bank v City of San Diego (1971) 19 CA3d 421, 97 CR 61: §11.57
Seeger v Odell (1941) 18 C2d 409, 115 P2d 977: §§6.73, 10.77
Seeley v Seymour (1987) 190 CA3d 844, 237 CR 282: §15.24
Sentinel Management Co. v New Hampshire Ins. Co. (Minn App 1997) 563 NW2d 296: §13.139
Serafini, U.S. v (MD Pa 1988) 706 F Supp 346: §7.25
Servco Pac., Inc. v Dods (D Haw 2000) 106 F Supp 2d 1034: §7.13
Sessions v Pacific Improvement Co. (1922) 57 CA 1, 206 P 653: §§2.99, 2.103
Severns v Union Pac. R.R. Co. (2002) 101 CA4th 1209, 125 CR2d 100: §§10.2, 11.15, 11.31, 11.49
Seymour v Shaeffer (1947) 82 CA2d 823, 187 P2d 95, disapproved on other grounds in Ellis v Mihelis (1963) 60 C2d 206, 32 CR 415: §§4.53, 4.122

Shade Foods, Inc. v Innovative Prods. Sales & Mktg., Inc. (2000) 78 CA4th 847, 93 CR2d 364: §§13.20, 13.112, 13.115, 13.117, 14.26, 14.68
Shapiro v Hu (1986) 188 CA3d 324, 233 CR 470: §§2.185, 6.9
Shapiro v Sutherland (1998) 64 CA4th 1534, 76 CR2d 101: §§2.187, 6.30-6.31
Shaver v Clanton (1994) 26 CA4th 568, 31 CR2d 595: §8.16
Shaw v Caldwell (1911) 16 CA 1, 115 P 941: §12.13
Shaw Mortgage Corp. v Peerless Ins. Co. (SD Cal 2009) 615 F Supp 2d 1172: §13.60
Shaw Mortgage, 615 F Supp 2d at 1175: §13.60
Shawmut Bank, N.A. v Kress Assoc. (9th Cir 1994) 33 F3d 1477: §9.5
Shell Oil Co. v National Union Fire Ins. Co. (1996) 44 CA4th 1633, 52 CR2d 580: §14.51
Shelley v Kraemer (1948) 334 US 1, 92 L Ed 1161, 68 S Ct 836: §4.66
Shepard v Edward Mackay Enters., Inc. (2007) 148 CA4th 1092, 56 CR3d 326: §6.18
Sherwood-Trimble Med. Group v 1001 Venice Blvd. Partnership (1999) 75 CA4th 872, 89 CR2d 533: §9.9
Shortell v Evans-Ferguson Corp. (1929) 98 CA 650, 277 P 519: §4.3
Shreeves v Pearson (1924) 194 C 699, 230 P 448: §15.18
Shugerman v Allstate Ins. Co. (CD Cal 2009) 594 F Supp 2d 1131: §§13.93, 13.95-13.96
Shugerman v Allstate Ins. Co. (CD Cal 2009) 594 F Supp2d 1131: §13.93
Siegel v Fidelity Nat'l Title Ins. Co. (1996) 46 CA4th 1181, 54 CR2d 84: §15.18
Sierra Pac. Indus. v Carter (1980) 104 CA3d 579, 163 CR 764: §§2.61, 2.161
Sierra Screw Prods. v Azusa Greens, Inc. (1979) 88 CA3d 358, 151 CR 799: §11.54
Silacci v Abrahamson (1996) 45 CA4th 558, 53 CR2d 37: §11.57
Siller v Board of Supervisors (1962) 58 C2d 479, 25 CR 73: §4.87
Simank Realty, Inc. v DeMarco (1970) 6 CA3d 610, 86 CR 212: §§2.81, 2.116
Simon v San Paolo U.S. Holding Co., Inc. (2005) 35 C4th 1159, 29 CR3d 379: §§13.118B, 13.118E
Simone v McKee (1956) 142 CA2d 307, 298 P2d 667: §§2.141, 2.155, 2.162
Sipper, People v (1943) 61 CA2d Supp 844, 142 P2d 960, disap-proved on other grounds in Murgia v Municipal Court (1975) 15 C3d 286, 124 CR 204: §2.147
Sisk v Caswell (1910) 14 CA 377, 112 P 185: §12.7
Sixells, LLC v Cannery Bus. Park (2008) 170 CA4th 648, 88 CR3d 235: §§4.92, 10.76, 11.24
Sixta v Ochsner (1960) 187 CA2d 485, 9 CR 617: §8.13
Sixth Dist. Agric. Ass'n v Wright (1908) 154 C 119, 97 P 144: §10.65
Skopp v Weaver (1976) 16 C3d 432, 128 CR 19: §§2.28, 2.132
Skycom Corp. v Telstar Corp. (7th Cir 1987) 813 F2d 810: §§3.19, 3.23, 3.26
Slater v Shell Oil Co. (1940) 39 CA2d 535, 3 CR 697: §11.62
Slottow v American Cas. Co. (9th Cir 1993) 10 F3d 1355: §13.115
Smiddy v Grafton (1912) 163 C 16, 124 P 433: §§9.45, 12.7
Smith v Coldwell Banker Real Estate Servs. (D Conn 2000) 122 F Supp 2d 267: §6.51
Smith v Fair Employment & Hous. Comm'n (1996) 12 C4th 1143, 51 CR2d 700: §2.181
Smith v Jim Dandy Markets, Inc. (9th Cir 1949) 172 F2d 616: §13.17
Smith v Mady (1983) 146 CA3d 129, 194 CR 42: §4.141
Smith v Renz (1954) 122 CA2d 535, 265 P2d 160: §9.45
Smith v Rickard (1988) 205 CA3d 1354, 254 CR 633: §2.159
Smith v Zak (1971) 20 CA3d 785, 98 CR 242: §§2.61, 2.132-2.133, 2.138, 4.135
Snapp v State Farm Fire & Cas. Co. (1962) 206 CA2d 827, 24 CR 44: §§13.69, 13.81
Snelson v Ondulando Highlands Corp. (1970) 5 CA3d 243, 84 CR 800: §6.31A
Snodgrass v Crane (1943) 57 CA2d 565, 134 P2d 862: §11.70
Snukal v Flightways Mfg., Inc. (2000) 23 C4th 754, 98 CR2d 1: §§4.28, 10.20
Soderling v Tomlin (1959) 170 CA2d 169, 338 P2d 946: §4.59
South Carolina Recycling & Disposal, Inc., U.S. v (D SC 1985) 653 F Supp 984, aff'd sub nom U.S. v Monsanto Co. (4th Cir 1988) 858 F2d 160: §7.13
Southdown v Allen (ND Ala 2000) 119 F Supp 2d 1223: §7.21
Southern Christian Leadership Conf. v Al Malaikah Auditorium Co. (1991) 230 CA3d 207, 281 CR 216: §§8.16, 9.53
Southern Pac. Co. v County of Riverside (1939) 35 CA2d 380, 95 P2d 688: §4.32
Southern Pac. Co. v Dore (1917) 34 CA 521, 168 P 147: §§12.5-12.6
Southern Pac. Land Co. v Meserve (1921) 186 C 157, 198 P 1055: §11.93
Southland Corp. v Keating (1984) 465 US 1, 79 L Ed 2d 1, 104 S Ct 852: §6.15
Southwest Concrete Prods. v Gosh Constr. Corp. (1990) 51 C3d 701, 274 CR 404: §9.6
Spangler v Castello (1956) 147 CA2d 49, 304 P2d 752: §4.3
Spangler v Memel (1972) 7 C3d 603, 102 CR 807: §§9.1, 9.71-9.72, 9.95-9.98
Sparks v Sparks (1950) 101 CA2d 129, 225 P2d 238: §4.15
Spaulding v Yovino-Young (1947) 30 C2d 138, 180 P2d 691: §§8.25, 8.57
Speck v Wylie (1934) 1 C2d 625, 36 P2d 618: §2.185
Spellman v Dixon (1967) 256 CA2d 1, 63 CR 668: §9.75
Spencer v Marshall (2008) 168 CA4th 783, 85 CR3d 752: §6.107
Spitler v Avery (1961) 189 CA2d 811, 11 CR 724: §2.45

Spray, Gould & Bowers v Associated Int'l Ins. Co. (1999) 71 CA4th 1260, 84 CR2d 552: §13.93
Spurgeon v Drumheller (1985) 174 CA3d 659, 220 CR 195: §4.141
St. James Armenian Church v Kurkjian (1975) 47 CA3d 547, 121 CR 214: §§2.135, 2.160
St. Louis v DeBon (1962) 204 CA2d 464, 22 CR 443: §11.68
St. Paul Fire & Marine Ins. Co. v Coss (1978) 80 CA3d 888, 145 CR 836: §§14.27, 14.64
St. Paul Title Co. v Meier (1986) 181 CA3d 948, 226 CR 538: §§9.5, 15.12
Stalberg v Western Title Ins. Co. (1994) 27 CA4th 925, 32 CR2d 750: §15.22
Stalberg v Western Title Ins. Co. (1991) 230 CA3d 1223, 282 CR 43: §15.22
Stamm Theatres, Inc. v Hartford Cas. Ins. Co. (2001) 93 CA4th 531, 113 CR2d 300: §13.86
Standard Fire Ins. Co. v Spectrum Community Ass'n (2006) 141 CA4th 1117, 46 CR3d 804: §14.49
Standard Realty & Dev. Co. v Ferrera (1957) 151 CA2d 514, 311 P2d 855: §2.38
Stanislaus Water Co. v Bachman (1908) 152 C 716, 93 P 858: §10.44
Starr v Mooslin (1971) 14 CA3d 988, 92 CR 583: §§9.4, 9.71
State v Agostini (1956) 139 CA2d 909, 294 P2d 769: §8.24
State Farm Fire & Cas. Co. v Superior Court (2008) 164 CA4th 317, 78 CR3d 828: §§14.53-14.54
State Farm Fire & Cas. Co. v Superior Court (1996) 45 CA4th 1093, 53 CR2d 229: §13.122
State Farm Fire & Cas. Co. v Superior Court (1989) 215 CA3d 1435, 264 CR 269: §§13.73, 13.138
State Farm Fire & Cas. Co. v Von Der Lieth (1991) 54 C3d 1123, 2 CR2d 183: §13.84
State Farm Fire & Casualty Co. v Von Der Lieth (1991) 54 C3d 1123, 2 CR2d 183: §13.83
State Farm Mut. Auto. Ins. Co. v Campbell (2003) 538 US 408, 155 L Ed 2d 585, 123 S Ct 1513: §§13.118-13.118A
State Farm Mut. Auto. Ins. Co. v Jacober (1973) 10 C3d 193, 110 CR 1: §§13.107, 14.35
State Farm Mut. Auto. Ins. Co. v Superior Court (1991) 228 CA3d 721, 279 CR 116: §13.120
State of Cal. ex rel State Lands Comm'n v Superior Court (1995) 11 C4th 50, 44 CR2d 399: §11.82
Stearns v Los Angeles Sch. Dist. (1966) 244 CA2d 696, 53 CR 482: §10.13
Stearns v Title Ins. & Trust Co. (1971) 18 CA3d 162, 95 CR 682: §15.87
Steiner v Rowley (1950) 35 C2d 713, 221 P2d 9: §2.26
Steiner v Thexton (review granted Sept. 17, 2008, S164928; superseded opinion at 163 CA4th 359, 77 CR3d 632): §§4.85, 5.12, 8.13
Steitz v Irwin (1949) 94 CA2d 871, 211 P2d 919: §10.75
Stephens v Ahrens (1919) 179 C 743, 178 P 863: §2.38
Stephens, Estate of (2002) 28 C4th 665, 122 CR2d 358: §10.55
Stephens, Partain & Cunningham v Hollis (1987) 196 CA3d 948, 242 CR 251: §2.126
Sterling v Taylor (2007) 40 C4th 757, 55 CR3d 116: §§2.44, 8.9
Stetler v Greenpoint Mortgage Funding Inc. (ED Cal, Jan. 23, 2008) 2008 US Dist Lexis 4880: §§2.38A, 2.135
Steve Schmidt & Co. v Berry (1986) 183 CA3d 1299, 228 CR 689: §2.113
Stevenson v Baum (1998) 65 CA4th 159, 75 CR2d 904: §§6.30-6.31, 6.32A, 6.73
Stewart v Truck Ins. Exch. (1993) 17 CA4th 468, 21 CR2d 338: §13.117A
Stickel v Harris (1987) 196 CA3d 575, 242 CR 88: §§2.9, 2.171
Stiles v Bodkin (1941) 43 CA2d 839, 111 P2d 675: §4.109
Stockwell v Lindeman (1964) 229 CA2d 750, 40 CR 555: §8.9
Stone v Hartford Cas. Co. (CD Cal 2006) 470 F Supp 2d 1088: §14.71
Stonecrest Corp. (1955) 24 TC 659, nonacq 1956-1 Cum Bull 6: §§9.29, 9.60
Stonelight Tile, Inc. v California Ins. Guarantee Ass'n (2007) 150 CA4th 19, 58 CR3d 74: §§14.47-14.48
Stonewall Ins. Co. v City of Palos Verdes Estates (1996) 46 CA4th 1810, 54 CR2d 176: §14.20
Storage Servs. v Oosterbaan (1989) 214 CA3d 498, 262 CR 689: §§6.31B, 6.73
Stough v Hanson (1941) 46 CA2d 504, 116 P2d 77: §8.11
Stout v Turney (1978) 22 C3d 718, 150 CR 637: §§2.155-2.156
Stowe v Nieto (1945) 71 CA2d 375, 162 P2d 837: §6.31A
Stratton v Tejani (1982) 139 CA3d 204, 187 CR 231: §4.149
Strebel v Brenlar Investments (2006) 135 CA4th 740, 37 CR3d 699: §2.155
Streiff v Darlington (1937) 9 C2d 42, 68 P2d 728: §6.106B
Strickland v Federal Ins. Co. (1988) 200 CA3d 792, 246 CR 345: §§13.69, 13.140
Stromer v Browning (1966) 65 C2d 421, 55 CR 18: §§2.76, 2.110, 4.12
Strong v Strong (1943) 22 C2d 540, 140 P2d 386: §10.55
Strong v Theis (1986) 187 CA3d 913, 232 CR 272: §§8.16, 8.27, 8.56
Stuart v Department of Real Estate (1983) 148 CA3d 1, 195 CR 524: §2.166
Stubble v United Servs. Auto. Ass'n (1973) 35 CA3d 498, 110 CR 828: §13.72
Suarez v Office of Admin. Hearings (2004) 123 CA4th 1191, 20 CR3d 618: §2.173
Sullivan v Little Hunting Part, Inc. (1969) 396 US 229, 24 L Ed 2d 386, 90 S Ct 400: §6.99
Summers v Freeman (1954) 128 CA2d 828, 276 P2d 131: §§2.58-2.59, 2.88
Summit Fin. Holdings, Ltd. v Continental Lawyers Title Co. (2002) 27 C4th 705, 117 CR2d 541: §§15.13, 15.18, 15.23
Sunset Drive Corp. v City of Redlands (1999) 73 CA4th 215, 86 CR2d 209: §4.95
Super 7 Motel Assocs. v Wang (1993) 16 CA4th 541, 20 CR2d 193: §2.158
Sutton v Warner (1993) 12 CA4th 415, 15 CR2d 632: §4.13
Swain v California Cas. Ins. Co. (2002) 99 CA4th 1, 120 CR2d 808: §14.21

Sweat v Hollister (1995) 37 CA4th 603, 43 CR2d 399, disapproved on other grounds in Santisas v Goodin (1998) 17 C4th 599, 71 CR2d 830: §6.32A
Sweat v Hollister (1995) 37 CA4th 603, 43 CR2d 399, overruled on other grounds in Santisas v Goodin (1998) 17 C4th 599, 71 CR2d 830: §2.127
Swiss Prop. Mgmt. Co. v Southern Cal. IBEW-NECA Pension Plan (1997) 60 CA4th 839, 70 CR2d 587: §§9.71, 9.80, 9.82
Szabo v Superior Court (1978) 84 CA3d 839, 148 CR 837: §12.4

T

T.M. Cobb Co. v Superior Court (1984) 36 C3d 273, 204 CR 143: §8.5
Tan v California Fed. Sav. & Loan Ass'n (1983) 140 CA3d 800, 189 CR 775: §9.52
Tandy v Waesch (1908) 154 C 108, 97 P 69: §§4.66, 12.14
Tanglewood E. Homeowners v Charles-Thomas, Inc. (5th Cir 1988) 849 F2d 1568: §§7.12, 7.14, 7.16
Tanner v Title Ins. & Trust Co. (1942) 20 C2d 814, 129 P2d 383: §10.44
Taormina Theosophical Community, Inc. v Silver (1983) 140 CA3d 964, 190 CR 38: §8.16
Tarrant v Butler (1960) 180 CA2d 235, 4 CR 230: §§6.72-6.73
Tate v Fratt (1896) 112 C 613, 44 P 1061: §4.65
Taylor v Coachella Valley County Water Dist. (1952) 108 CA2d 743, 239 P2d 454: §§10.4, 12.10
Teachers Ins. & Annuity Ass'n v Furlotti (1999) 70 CA4th 1487, 83 CR2d 455: §11.43
Teachers Ins. & Annuity Ass'n v Tribune Co. (SD NY 1987) 670 F Supp 491: §§3.16-3.17, 3.19, 3.22-3.23, 3.30
Temple v Kerwin (1989) 209 CA3d 1087, 257 CR 651: §2.169
Tennant v John Tennant Memorial Home (1914) 167 C 570, 140 P 242: §10.52
Tenzer v Superscope, Inc. (1985) 39 C3d 18, 216 CR 130: §§2.5, 2.50-2.51, 2.94
Tetrick v Sloan (1959) 170 CA2d 540, 339 P2d 613: §§2.54, 2.59
Texaco, Inc. v Pennzoil Co. (Tex App 1987) 729 SW2d 768: §§3.19-3.20, 3.22-3.24
Textron Fin. Corp. v National Union Fire Ins. Co. (2004) 118 CA4th 1061, 13 CR3d 586: §§13.115, 13.118B, 13.122
Textron Financial Corp. v National Union Fire Ins. Co. (2004) 118 CA4th 1061, 13 CR3d 586: §13.117B
Thaler v Household Fin. Corp. (2000) 80 CA4th 1093, 95 CR2d 779: §8.18
Thomas v Anchorage Equal Rights Comm'n (9th Cir 2000) 220 F3d 1134: §2.181
Thomas v Anchorage Equal Rights Comm'n (9th Cir 1999) 165 F3d 692: §2.181
Thomas v Witte (1963) 214 CA2d 322, 29 CR 412: §4.23
Thompson v Allert (1991) 233 CA3d 1462, 285 CR 367: §9.98
Thompson v Liquichimica of Am. (SD NY 1979) 481 F Supp 365: §3.28
Thompson v Mercury Cas. Co. (2000) 84 CA4th 90, 100 CR2d 596: §13.74
Thompson v Schurman (1944) 65 CA2d 432, 150 P2d 509: §4.13
Thompson v Toll Dublin, LLC (2008) 165 CA4th 1360, 81 CR3d 736: §6.15
Thompson, People v (1954) 43 C2d 13, 271 P2d 507: §11.25
Thomson v International Alliance of Theatrical Stage Employees (1965) 232 CA2d 446, 42 CR 785: §3.26
Timmsen v Forest E. Olson, Inc. (1970) 6 CA3d 860, 86 CR 359: §2.143
Tinker v McLellan (1958) 165 CA2d 291, 331 P2d 464: §13.14
Toews v U.S. (2004) 376 F3d 1371: §11.50
Tomaselli v Transamerica Ins. Co. (1994) 25 CA4th 1269, 31 CR2d 433: §§13.80, 13.117
Topanga Ass'n for a Scenic Community v County of Los Angeles (1974) 11 C3d 506, 113 CR 836: §4.87
Torelli v J.P. Enters. (1997) 52 CA4th 1250, 61 CR2d 76: §§2.48, 2.52, 2.115
Torlai v Lee (1969) 270 CA2d 854, 76 CR 239: §§8.10-8.11
Tosco Corp. v General Ins. Co. (2000) 85 CA4th 1016, 102 CR2d 657: §14.50
Track Mortgage Group, Inc. v Crusader Ins. Co. (2002) 98 CA4th 857, 120 CR2d 228: §§13.31-13.32, 13.115
Tract Dev. Servs., Inc. v Kepler (1988) 199 CA3d 1374, 246 CR 469: §§11.46, 11.62
Tradewinds Escrow, Inc. v Truck Ins. Exch. (2002) 97 CA4th 704, 118 CR2d 561: §14.71
Tran v Farmers Group, Inc. (2002) 104 CA4th 1202, 128 CR2d 728: §13.121
Travelers Cas. & Sur. Co. v Superior Court (1998) 63 CA4th 1440, 75 CR2d 54: §13.76
Travelers Ins. Co. v Lesher (1986) 187 CA3d 169, 231 CR 791, disapproved on other grounds in Buss v Superior Court (1997) 16 C4th 35, 65 CR2d 366: §13.112
Triple A Mgmt. Co. v Frisone (1999) 69 CA4th 520, 81 CR2d 669: §§10.2, 12.2, 15.20, 15.86
Tropico Land & Improvement Co. v Lambourn (1915) 170 C 33, 148 P 206: §12.9
Trout v Taylor (1934) 220 C 652, 32 P2d 968: §10.76
Truman Bowen (1949) 12 TC 446, acq 1951-2 Cum Bull 1: §9.21
Trust One Mortgage Corp. v Invest Am. Mortgage Corp. (2005) 134 CA4th 1302, 37 CR3d 83: §2.163
Truta v Avis Rent-A-Car Sys. (1987) 193 CA3d 802, 238 CR 806: §13.81
Tucker v American Ins. Co. (1932) 123 CA 316, 11 P2d 55: §13.24
Tucker v Lassen Sav. & Loan Ass'n (1974) 12 C3d 629, 116 CR 633: §9.16
Tusher v Gabrielsen (1998) 68 CA4th 131, 80 CR2d 126: §§10.2, 11.54
Tustin Heights Ass'n v Board of Supervisors (1959) 170 CA2d 619, 339 P2d 914: §4.87
Tyrone v Kelley (1973) 9 C3d 1, 106 CR 761: §2.5

U

U.S. v _____ (*see* name of defendant)
U.S. Hertz, Inc. v Niobrara Farms (1974) 41 CA3d 68, 116 CR 44: §15.89
USA, Inc. (2008) 159 CA4th 655, 71 CR3d 775: §13.118
USF Ins. Co. v Clarendon America Ins. Co. (CD Cal 2006) 452 F Supp 2d 972: §§14.49B-14.49C
Ulrich v State Farm Fire & Cas. Co. (2003) 109 CA4th 598, 135 CR2d 131: §14.19
Union Transp. Co. v Sacramento County (1954) 42 C2d 235, 267 P2d 10: §11.77
United States Bldg. & Loan Ass'n v Salisbury (1932) 217 C 35, 17 P2d 140: §9.85
University of Judaism v Transamerica Ins. Co. (1976) 61 CA3d 937, 132 CR 907: §13.24
Unsecured Creditors' Comm. of Robert L. Helms Constr. & Dev. Co. v Southmark Corp. (In re Robert L. Helms Constr. & Dev. Co.) (9th Cir 1998) 139 F3d 702: §8.28

V

Van Core v Bodner (1947) 77 CA2d 842, 176 P2d 784: §10.76
Van Holt v Liberty Mut. Ins. Co. (3rd Cir 1998) 163 F3d 161: §13.53
Van Klompenburg v Berghold (2005) 126 CA4th 345, 23 CR3d 799: §11.66
Van Sicklen v Browne (1971) 15 CA3d 122, 92 CR 786: §§4.86-4.87
Van Slyke v Arrowhead Reservoir & Power Co. (1909) 155 C 675, 102 P 816: §11.73
Vance v Pena (1871) 41 C 686: §12.16
Vargas v Hampson (1962) 57 C2d 479, 20 CR 618: §2.181
Varwig v Anderson-Behel Porsche/Audi, Inc. (1977) 74 CA3d 578, 141 CR 539: §2.187
Vella v Ratto (1971) 17 CA3d 737, 95 CR 72: §11.78
Venable v Harmon (1965) 233 CA2d 297, 43 CR 490: §§9.14, 9.16
Venoco, Inc. v Gulf Underwriters Ins. Co. (2009) 175 CA4th 750, 96 CR3d 409: §§14.53, 14.68A
Venture Assoc. v Zenith Data Sys. (7th Cir 1996) 96 F3d 275: §3.29
Verbeck v Clymer (1927) 202 C 557, 261 P 1017: §9.6
Vestar Dev. II v General Dynamics Corp. (9th Cir 2001) 249 F3d 958: §§3.27-3.29
Vezaldenos v Keller (1967) 254 CA2d 816, 62 CR 808: §11.15
Vierneisel v Rhode Island Ins. Co. (1946) 77 CA2d 229, 175 P2d 63: §§9.53, 13.24
Vikco Ins. Servs., Inc. v Ohio Indemn. Co. (1999) 70 CA4th 55, 82 CR2d 442: §2.171
Vilkin v Sommer (1968) 260 CA2d 687, 67 CR 837: §9.105
Villacreses v Molinari (2005) 132 CA4th 1223, 34 CR3d 281: §6.16
Vincent v Garland (1936) 14 CA2d 725, 58 P2d 1320: §4.42
Vincent E. Webb (1987) TC Memo 1987-451: §9.29
Vinci v Edmonds (1986) 185 CA3d 1251, 230 CR 308: §2.167
Virginia Iron, Coal & Coke Co. v Commissioner (4th Cir 1938) 99 F2d 919: §8.35
Virtanen v O'Connell (2006) 140 CA4th 688, 44 CR3d 702: §15.26
Vitton Constr. Co. v Pacific Ins. Co. (2003) 110 CA4th 762, 2 CR3d 1: §14.43
Voight, Floyd J. (1977) 68 TC 99, aff'd (5th Cir 1980) 614 F2d 94: §9.59
Volf v Ocean Acc. & Guar. Corp. (1958) 50 C2d 373, 325 P2d 987: §§14.62, 14.65
Votypka v Valentine (1919) 41 CA 74, 182 P 76: §15.90
Vournas v Fidelity Nat'l Title Ins. Co. (1999) 73 CA4th 668, 86 CR2d 490: §15.18
Vu v Prudential Prop. & Cas. Ins. Co. (2001) 26 C4th 1142, 113 CR2d 70: §§13.93, 13.121

W

Wachovia Bank v Lifetime Indus. (2006) 145 CA4th 1039, 52 CR3d 168: §§8.18, 8.21, 8.55
Waggle v Worthy (1887) 74 C 266, 15 P 831: §12.14
Wagner Seed Co. v Daggett (ED NY 1986) 1986 US Dist Lexis 30030, aff'd (2d Cir 1986) 800 F2d 310: §7.15
Wagnerv O'Bannon (1969) 274 CA2d 121, 79 CR 44: §2.181
Wakefield v Bohlin (2006) 145 CA4th 963, 52 CR3d 400: §2.158
Walbridge v Richards (1931) 212 C 408, 298 P 971: §4.13
Waldsmith v State Farm Fire & Cas. Co. (1991) 232 CA3d 693, 283 CR 607: §13.86
Waldteufel v Sailor (1944) 62 CA2d 577, 144 P2d 894: §2.53
Walker v Farmers Ins. Exch. (2007) 153 CA4th 965, 63 CR3d 507: §13.118B
Wallace v Imbertson (1961) 197 CA2d 392, 17 CR 117: §8.57
Wallace v Onate (1991) 2 CA4th 549, 3 CR2d 3: §2.167
Waller v Truck Ins. Exch. (1995) 11 C4th 1, 44 CR2d 370: §§13.112, 14.25, 14.29-14.30, 14.53-14.54
Walner v City of Turlock (1964) 230 CA2d 399, 41 CR 29: §11.60
Walsh v Hooker & Fay (1963) 212 CA2d 450, 28 CR 16: §2.163
Walters v Marler (1978) 83 CA3d 1, 147 CR 655: §§2.157-2.158, 2.178
Ward v De Oca (1898) 120 C 102, 52 P 130: §4.42
Ward v Taggart (1959) 51 C2d 736, 336 P2d 534: §§2.124, 2.155, 2.157, 2.160, 2.162, 2.177
Ward Gen. Ins. Servs., Inc. v Employers Fire Ins. Co. (2003) 114 CA4th 548, 7 CR3d 844: §13.73
Ware v Security-First Nat'l Bank (1936) 7 C2d 604, 61 P2d 936: §13.11
Warfield v Peninsula Golf & Country Club (1995) 10 C4th 594, 42 CR2d 50: §6.101
Warington Lumber Co. v Fullerton Mortgage & Escrow Co. (1963) 222 CA2d 706, 35 CR 423: §15.30

Warner v Fire Ins. Exch. (1991) 230 CA3d 1029, 281 CR 635: §§13.19, 14.25
Warner Bros. Pictures v Brodel (1948) 31 C2d 766, 192 P2d 949: §§8.5, 9.53
Warren v Atchison, T. & S.F. Ry. (1971) 19 CA3d 24, 96 CR 317: §§10.13, 10.28
Warren v Merrill (2006) 143 CA4th 96, 49 CR3d 122: §§2.155, 10.19
Warshauer v Bauer Constr. Co. (1960) 179 CA2d 44, 3 CR 570: §§2.67, 2.184
Washington v Time Oil Co. (WD Wash 1988) 687 F Supp 529: §7.23
Washington Mut. Bank v Superior Court (2002) 95 CA4th 606, 115 CR2d 765: §15.74
Wasmann v Seidenberg (1988) 202 CA3d 752, 248 CR 744: §§15.2, 15.26
Waters v United Servs. Auto. Ass'n (1996) 41 CA4th 1063, 48 CR2d 910: §13.112
Watt v Patterson (1954) 125 CA2d 788, 271 P2d 200: §6.30
Watts v Farmers Ins. Exch. (2002) 98 CA4th 1246, 120 CR2d 694: §13.30
Watts, Estate of (1984) 162 CA3d 1160, 208 CR 846: §8.27
Watts, In re (Bankr ND Cal 2000) 244 BR 823: §8.15
Watts Indus., Inc. v Zurich Am. Ins. Co. (2004) 121 CA4th 1029, 18 CR3d 61: §§14.26, 14.49, 14.66, 14.68
Weaver, Marriage of (2005) 127 CA4th 858, 26 CR3d 121: §10.33
Webb, Vincent E., (1987) TC Memo 1987-451: §9.29
Webber v Inland Empire Invs., Inc. (1999) 74 CA4th 884, 88 CR2d 594: §9.97
Weber v Ross (1958) 159 CA2d 77, 323 P2d 465: §2.109
Wedge v Security First Nat'l Bank (1933) 219 C 113, 25 P2d 411: §2.186
Weiner v Mullaney (1943) 59 CA2d 620, 140 P2d 704: §4.12
Weisman, In re (9th Cir 1993) 5 F3d 417: §11.11
Weiss v Brentwood Sav. & Loan Ass'n (1970) 4 CA3d 738, 84 CR 736: §§9.76, 9.85
Welch v Kai (1970) 4 CA3d 374, 84 CR 619: §11.65
Wellenkamp v Bank of America (1978) 21 C3d 943, 148 CR 379: §§9.16, 9.50
Wells Fargo Bank v Town of Woodside (1983) 33 C3d 379, 189 CR 41: §1.79
Wesley N. Taylor Co. v Russell (1961) 194 CA2d 816, 15 CR 357: §2.109
West v State Farm Fire & Cas. Co. (9th Cir 1988) 868 F2d 348: §13.92
West v Superior Court (1994) 27 CA4th 1625, 34 CR2d 409: §2.183
Western Aggregates, Inc. v County of Yuba (2002) 101 CA4th 278, 130 CR2d 436: §§11.30, 11.77
Western Employers Ins. Co. v Arciero & Sons, Inc. (1983) 146 CA3d 1027, 194 CR 688: §14.63
Western Filter Corp. v Argan, Inc. (9th Cir 2008) 540 F3d 947: §4.109
Western Fire Ins. Co. v First Presbyterian Church (Colo 1968) 437 P2d 52: §13.73
Western Mut. Ins. Co. v Yamamoto (1994) 29 CA4th 1474, 35 CR2d 698: §14.35
Westfield Ins. Co. v Sheehan Constr. Co., Inc. (SD Ind 2008) 580 F Supp 2d 701, aff'd (7th Cir 2009) 564 F3d 817: §14.49B
Westlake v Silva (1942) 49 CA2d 476, 121 P2d 872: §11.108
Westoil Terminals Co. v Industrial Indem. Co. (2003) 110 CA4th 139, 1 CR3d 516: §14.49C
Westoil Terminals Co., Inc. v Industrial Indemnity Co. (2003) 110 CA4th 139, 1 CR3d 516: §14.55
Westra v Marcus & Millichap Real Estate Inv. Brokerage Co. (2005) 129 CA4th 759, 28 CR3d 752: §2.154
Westrec Marina Mgmt., Inc. v Arrowood Indem. Co. (2008) 163 CA4th 1387, 78 CR3d 264: §§14.13, 14.14A
Wheat v Morse (1961) 197 CA2d 203, 17 CR 226: §8.11
White v Schader (1921) 185 C 606, 198 P 19: §4.41
White v State (1971) 21 CA3d 738, 99 CR 58: §11.15
White v Ultramar, Inc. (1999) 21 C4th 563, 88 CR2d 19: §13.117B
White v Western Title Ins. Co. (1985) 40 C3d 870, 221 CR 509: §§4.55, 13.119
White & Bollard, Inc. v Goodenow (Wash 1961) 361 P2d 571: §4.3
White Point Co. v Herrington (1968) 268 CA2d 458, 73 CR 885: §§9.100-9.102
Whiteman v Leonard Realty Co. (1961) 189 CA2d 373, 11 CR 211: §2.38
Whiting, In re (2004) 311 BR 539: §11.11
Whitney Estate Co. v Northern Assur. Co. (1909) 155 C 521, 101 P 911: §13.23
Whitney Inv. Co. v Westview Dev. Co. (1969) 273 CA2d 594, 78 CR 302: §§2.83, 2.148
Wholey v Cavanaugh (1891) 88 C 132, 25 P 1112: §§12.10, 12.16
Wiegmann & Rose Int'l Corp. v NL Indus. (ND Cal 1990) 735 F Supp 957: §7.64
Wilbur v Wilson (1960) 179 CA2d 314, 3 CR 770: §4.59
Willard v First Church of Christ, Scientist (1972) 7 C3d 473, 102 CR 739: §11.65
William Kent Estate Co., People v (1966) 242 CA2d 156, 51 CR 215: §11.82
Williams v Fassler (1980) 110 CA3d 7, 167 CR 545: §§9.31, 9.45
Williams v Marshall (1951) 37 C2d 445, 235 P2d 372: §4.59
Williams v United Cal. Bank (1963) 223 CA2d 309, 35 CR 788: §2.98
Williams v Wells & Bennett Realtors (1997) 52 CA4th 857, 61 CR2d 34: §2.178
Williams Plumbing Co. v Sinsley (1975) 53 CA3d 1027, 126 CR 345: §4.152
Williamson & Vollmer Eng'g, Inc. v Sequoia Ins. Co. (1976) 64 CA3d 261, 134 CR 427: §14.14A
Willig v Gold (1946) 75 CA2d 809, 171 P2d 754: §2.178
Wilson v Abrams (1969) 1 CA3d 1030, 82 CR 272: §11.70
Wilson v Century 21 Great W. Realty (1993) 15 CA4th 298, 18 CR2d 779: §§2.185, 6.9
Wilson v Farmers Ins. Exch. (2002) 102 CA4th 1171, 126 CR2d 305: §§13.86, 14.21

Wilson v Gentile (1992) 8 CA4th 759, 10 CR2d 713: §8.21
Wilson v Hisey (1957) 147 CA2d 433, 305 P2d 686: §§2.142, 2.144
Wilson v Nichols (1940) 39 CA2d 527, 103 P2d 1007: §15.86
Wilson v Pacific Coast Title Ins. Co. (1951) 106 CA2d 599, 235 P2d 431: §4.50
Wilson v White (1890) 84 C 239, 24 P 114: §10.25
Wilson, Estate of (1940) 40 CA2d 229, 104 P2d 716: §12.10
Wiltrakis v Wiltrakis (1966) 244 CA2d 257, 53 CR 97: §4.19
Winchell v English (1976) 62 CA3d 125, 133 CR 20: §6.101
Winnett v Roberts (1986) 179 CA3d 909, 225 CR 82: §2.9
Winslow v City of Vallejo (1906) 148 C 723, 84 P 191: §11.51
Wise v Clapper (1968) 257 CA2d 770, 65 CR 231: §4.41
Wise v Radis (1925) 74 CA 765, 242 P 90: §2.94
Wolf v Price (1966) 244 CA2d 165, 52 CR 889: §§2.38, 2.46, 4.71
Wood v Kalbaugh (1974) 39 CA3d 926, 114 CR 673: §6.32
Wood, Estate of (1973) 32 CA3d 862, 108 CR 522: §10.52
Woodbridge Realty v Plymouth Dev. Corp. (1955) 130 CA2d 270, 278 P2d 713: §2.102
Woodland Hills Residents Ass'n v City Council (1975) 44 CA3d 825, 118 CR 856: §1.76
Woods v Bennett (1919) 40 CA 34, 180 P 25: §12.18
Woods v Bradford (1967) 254 CA2d 501, 62 CR 391: §8.15
Woods v Superior Court (1983) 149 CA3d 931, 197 CR 185: §1.11
Woods-Drake v Lundy (5th Cir 1982) 667 F2d 1198: §6.99
Woodson, People v (1947) 78 CA2d 132, 177 P2d 586: §2.11
Woodward v Brown (1897) 119 C 283, 51 P 542: §§4.41, 9.100
Woodworth v Redwood Empire Sav. & Loan Ass'n (1971) 22 CA3d 347, 99 CR 373: §9.75
Woolls v Superior Court (2005) 127 CA4th 197, 25 CR3d 426: §6.18
World Exhibit Corp. v City Bank Farmers Trust Co. (App Div 1946) 61 NYS2d 889, aff'd (1946) 296 NY 586, 68 NE2d 876: §§4.137, 13.13
World Health & Education Foundation v Carolina Cas. Ins. Co. (ND Cal 2009) 612 F Supp 2d 1089: §§14.13, 14.15
World Indus., Inc. v Aetna Cas. & Sur. Co. (1996) 45 CA4th 1, 52 CR2d 690: §14.26
Wright v Boggess (1914) 24 CA 533, 141 P 1082: §§12.7, 12.18
Wright v Buzzine (1960) 180 CA2d 426, 4 CR 482: §2.109
Wright v Lowe (1956) 140 CA2d 891, 296 P2d 34: §2.38
Wright v Williams (1975) 47 CA3d 802, 121 CR 194: §1.14
Wyatt v Union Mortgage Co. (1979) 24 C3d 773, 157 CR 392: §2.8

X

Xuereb v Marcus & Millichap, Inc. (1992) 3 CA4th 1338, 5 CR2d 154: §2.158

Y

Yackey v Pacifica Dev. Co. (1979) 99 CA3d 776, 160 CR 430: §9.102
Yale Univ. v CIGNA Ins. Co. (D Conn 2002) 224 FSupp2d 402: §13.139
Yano, Estate of (1922) 188 C 645, 206 P 995: §§4.15, 10.24
Yeoman v Sawyer (1950) 99 CA2d 43, 221 P2d 225: §10.40
Yergan v Department of Real Estate (2000) 77 CA4th 959, 92 CR2d 189: §2.166
Yoakum v Tarver (1967) 256 CA2d 202, 64 CR 7: §2.109
Young v Blakeman (1908) 153 C 477, 95 P 888: §11.78

Z

Zack's, Inc. v City of Sausalito (2008) 165 CA4th 1163, 81 CR3d 797: §11.30
Zakessian v City of Sausalito (1972) 28 CA3d 794, 105 CR 105: §4.87
Zalk v General Exploration Co. (1980) 105 CA3d 786, 164 CR 647: §2.44
Zander v Texaco, Inc. (1968) 259 CA2d 793, 66 CR 561: §2.28
Zands v Nelson (SD Cal 1991) 779 F Supp 1254: §7.8
Zanelli v McGrath (2008) 166 CA4th 615, 82 CR3d 835: §11.59
Zang v Northwestern Title Co. (1982) 135 CA3d 159, 185 CR 176: §§15.7, 15.18
Zappas v King Williams Press, Inc. (1970) 10 CA3d 768, 89 CR 307: §2.5
Zelkowitz v Tobin (1951) 108 CA2d 69, 238 P2d 19: §2.98
Ziegler v Barnes (1988) 200 CA3d 224, 246 CR 69: §9.96
Zikratch v Stillwell (1961) 196 CA2d 535, 16 CR 660: §2.127
Zimmer v Dykstra (1974) 39 CA3d 422, 114 CR 380: §11.63
Zimmerman v Bank of America (1961) 191 CA2d 55, 12 CR 319: §§2.48, 2.121
Zinneman v Bagnol (2002) 104 CA4th 656, 128 CR2d 342: §2.168
Ziswasser v Cole & Cowan, Inc. (1985) 164 CA3d 417, 210 CR 428: §2.161
Zlozower v Lindenbaum (1929) 100 CA 766, 281 P 102: §§4.64, 4.66

88 Ops Cal Atty Gen 203 (2005): §2.94
84 Ops Cal Atty Gen 141: §4.81
79 Ops Cal Atty Gen 112 (1996): §6.33
73 Ops Cal Atty Gen 58, 67 (1990): §6.33
58 Ops Cal Atty Gen 408 (1975): §9.103
56 Ops Cal Atty Gen 496 (1973): §9.103
56 Ops Cal Atty Gen 404 (1973): §4.95
54 Ops Cal Atty Gen 13 (1971): §2.22
53 Ops Cal Atty Gen 196 (1970): §2.181
44 Ops Cal Atty Gen 105 (1964): §2.22
43 Ops Cal Atty Gen 284 (1964): §2.22
43 Ops Cal Atty Gen 19, 22 (1964): §9.91
43 Ops Cal Atty Gen 19 (1964): §9.94
13 Ops Cal Atty Gen 185, 187 (1949): §15.92

© The Regents of the University of California

Table of References

Advising California Common Interest Communities (Cal CEB 2003): §§6.46A, 6.60, 6.64, 6.98, 10.49, 11.7 12.1
Advising California Employers and Employees (Cal CEB 2005): §5.18
Advising California Partnerships (3d ed Cal CEB 1999): §§1.96, 4.24-4.26, 10.18, 10.64, App B
Augustine, Don & Stanton H. Zarrow. California Real Estate Law and Practice. New York, Matthew Bender, 2007: §§2.102, 8.35
Belsheim, Edmund O. Modern Legal Forms. Kansas City, Mo., and St. Paul, Vernon Law Book and West Publishing, 1979: §4.65
Bittker, Boris I. & Lawrence Lokken. Federal Taxation of Income, Estates and Gifts. 3d ed. Boston, Warren, Gorham & Lamont, 1999: §§8.34-8.35
Black's Law Dictionary. 8th ed. St. Paul, West Publishing, 2004: §§12.1, 12.9, 15.1
Bowman, Arthur G. & William D. Milligan. Real Estate Law in California. 10th ed. Englewood Cliffs, N.J., Prentice-Hall, 2000: §11.37
Brown, Curtis M., Walter G. Robillard, & Donald A. Wilson. Evidence and Procedures for Boundary Location. 3d ed. New York, Wiley, 1994: §§11.17, 11.39
California Administrative Mandamus (3d ed Cal CEB 2003): §2.173
California Attorney's Guide to Damages (2d ed Cal CEB 2004): §2.157
California Conservatorship Practice. 2 vols (Cal CEB 2005): §4.17
California Construction Contracts, Defects, and Litigation (Cal CEB 2008): §§1.78, 13.44, 13.70, 14.58
1, 3 California Decedent Estate Practice. Vols 1-2 (Cal CEB 1986): §§4.19, 10.22, 10.63
California Easements and Boundaries: Law and Litigation (Cal CEB 2008): §§10.2, 11.4, 11.6, 11.9, 11.25, 11.31, 11.43-11.44, 11.54-11.57, 11.59-11.62, 11.64-11.67, 11.70-11.75, 11.77-11.78, 11.80-11.81
California Land Use Practice (Cal CEB 2006): §§1.77-1.78, 1.84, 1.86, 4.86-4.88, 8.29, 8.46-8.47, 10.2
California Landlord-Tenant Practice. 2 vols (2d ed Cal CEB 1997): §§1.80, 2.181, 4.72, 6.98
California Liability Insurance Practice: Claims & Litigation. 2 vols (Cal CEB 1991): §§4.78, 13.82, 13.122, 14.1
California Mechanics' Liens and Related Construction Remedies (3d ed Cal CEB 1998): §§4.69, 4.78, 5.12, 9.80
California Mortgages, Deeds of Trust, and Foreclosure Litigation (4th ed Cal CEB 2009): §§4.33, 4.41, 4.43, 6.106A-6.106B, 7.88, 7.90, 7.93, 7.95, 8.54-8.55, 9.6-9.7, 9.9, 9.16, 9.21-9.22, 9.45, 9.47-9.49, 9.55-9.57, 9.68, 10.41, 13.26, 13.31-13.32
California Opinion Reports. Executive Committees of the Business Law and the Real Property Law Sections of the California State Bar, 2002: §§1.122, 1.128-1.130
California Powers of Attorney and Health Care Directives. 2 vols (Cal CEB 2008): §10.60
California Real Estate Brokers: Law and Litigation (Cal CEB 2009): §§2.1, 2.26, 2.43, 2.85, 2.91, 2.124, 2.152, 2.171, 2.184
California Real Estate Finance Practice: Strategies and Forms (Cal CEB 2000): §§1.29, 1.96, 1.130, 4.20, 4.40, 4.83, 4.181, 7.82, 9.3, 9.6, 9.22, 9.30, 9.47, 9.67, App B
California Real Property Remedies and Damages (2d ed Cal CEB 2002): §§1.100, 2.64, 3.26, 4.8-4.9, 4.49, 4.66, 4.83, 4.100, 4.116, 4.140-4.141, 4.143, 4.145-4.147, 4.149-4.150, 6.10, 6.30, 10.43, 11.15, 11.90, 11.118
California Subdivision Map Act and the Development Process (2d ed Cal CEB 2001): §§1.79, 1.83-1.84, 4.86, 4.92-4.93, 4.114, 9.103, 11.24
California Title Insurance Practice (2d ed Cal CEB 1997): §§1.17, 1.61, 1.65, 1.116, 1.132-1.139, 1.142, 2.135, 4.24, 4.28, 4.39, 4.51, 4.53-4.59, 4.63-4.64, 4.67-4.71, 4.90, 4.92, 4.111, 4.113-4.114, 4.122, 4.174, 6.66, 6.79-6.83, 6.85, 7.37, 7.86, 8.19, 9.43, 9.80, 9.100, 10.56, 11.2, 11.10-11.13, 11.75, 12.3, 13.122, 15.8, 15.13, 15.15, 15.36, 15.40, 15.74, 15.91, App B
California UCC Sales and Leases (Cal CEB 2002): §§5.10, 5.12, 5.23
Casner, A. James, ed., American Law of Property : A Treatise on the Law of Property in the United States. Boston, Little, Brown, 1952: §§4.65, 12.7, 12.9, 12.12-12.13
Cherkis, Lawrence. Collier Real Estate Transactions and the Bankruptcy Code. New York, Matthew Bender, 1992: §8.28
Condemnation Practice in California. 2 vols (3d ed Cal CEB 2005): §§9.110, 11.87
Drafting Business Contracts: Principles, Techniques & Forms (Cal CEB 1994): §§2.86, 3.35, 4.3, 6.21
Drafting California Revocable Trusts (4th ed Cal CEB 2003): §6.80
Ehrman, Kenneth A. & Sean Flavin. Taxing California Property. 3d ed. St. Paul, West Publishing, 1988: §4.60
Environmental Aspects of Real Estate Transactions, Section of Natural Resources, Energy, and Environmental Law and Section of Real Property, Probate, and Trust Law. American Bar Association, 1995: §7.1
Eyster, James J. The Negotiation and Administration of Hotel and Restaurant Management Contracts. 3d ed. Ithaca, NY, Cornell University School of Hotel Administration, 1988: §5.3
Fee Agreement Forms Manual (2d ed Cal CEB 2007): §1.19
Forming and Operating California Limited Liability Companies (2d ed Cal CEB 2007): §§1.96, 4.27
Forming California Common Interest Developments (Cal CEB 2004): §§1.91, 5.7, 6.60, 6.64, 6.103, 11.7
Geltman, Elizabeth Glass. Prospective Purchaser Agreements: Reducing the Liability Risks of Contaminated Property. Chicago, ABA, 1997: §7.1
Gerrard, Michael B. Brownfields Law and Practice: The Cleanup and Redevelopment of Contaminated Land. 3 vols. New York, Matthew Bender, 1998: §7.1

Glazer, Donald W., Scott FitzGibbon & Steven O. Weise. Glazer and FitzGibbon on Legal Opinions. 2d ed. New York, Aspen Law & Business, 2001: §1.127
Grossman, Harvey M. & Arvo Van Alstyne. Pleading—Civil Actions. Vol 8. 2d ed. St. Paul, West Publishing, 1981: §11.90
Ground Lease Practice (2d ed Cal CEB 2009): §§1.27, 1.34, 4.75, 8.57
Hanna, John Paul, and David M. Van Atta. California Common Interest Developments: Law and Practice: A Guide to California Common Interest Development and Community Association Law. 2d ed. St. Paul, Minn., West, 2002: §5.7
Higgins, Jr., John E. The Developing Labor Law: The Board, the Courts, and the National Labor Relations Act. 5th ed. Washington, D.C., Bureau of National Affairs, 2006: §5.18
Hotels 2006: Acquiring, Managing, Developing & Converting the Hot Property. New York, Practising Law Institute, 2006: §5.1
Jackson, Kenneth T. The Crabgrass Frontier: The Suburbanization of the United States. New York, Oxford University Press, 1985: §11.1
Legal Opinions in Business Transactions (2005 Report). Business Law Section of the State Bar of California, 2005: §§1.122-1.124, 1.126-1.128
Litigator's Guide to Effective Use of ADR in California (Cal CEB 2005): §§4.150, 6.15
Lord, Richard A. Williston on Contracts. 4th ed. St. Paul, West Group, 1990-2000: §13.6
Mallen, Ronald E. & Jeffrey M. Smith. Legal Malpractice. 5 vols. St. Paul, West Publishing, 2007: §§1.15-1.16
Managing Asbestos in Place, A Building Owner's Guide to Operations and Maintenance Programs for Asbestos-Containing Materials. Washington, D.C., U.S. Environmental Protection Agency, 1990: §7.5
Manual of Instructions for the Survey of the Public Lands of the United States. Bureau of Land Management, 1973: §§11.17, 11.93
Miller, Harry D. & Marvin B. Starr. California Real Estate. 8 vols. 3d ed. San Francisco, Bancroft-Whitney, 2000: §§2.5, 2.74, 2.98, 2.129, 2.147, 4.51-4.52, 4.60, 4.77, 4.92, 4.152, 9.7, 9.59, 9.68, 9.70-9.71, 9.76, 9.83, 9.88, 10.5, 11.2, 12.2
Moskowitz, Joel S. Environmental Liability and Real Property Transactions: Law & Practice. 2d ed. New York, Wiley, 1995: §7.1
National Association of Realtors. Code of Ethics and Standards of Practice: §2.175
Office Leasing: Drafting and Negotiating the Lease. 2 vols (Cal CEB 1996): §§1.34, 4.72-4.73, 8.12, 8.57, 9.18, 9.21, 15.39, 15.65
Organizing Corporations in California (3d ed Cal CEB 2001): §1.96
Pomeroy, John Norton, Jr. & John C. Mann. Specific Performance of Contracts. 3d ed. Albany, N.Y., Banks & Co., 1926: §9.107
Powell, Richard R. The Law of Real Property. New York, Matthew Bender, 1986: §4.65
Practice Under the California Environmental Quality Act (2d ed Cal CEB 2008): §§1.82, 4.86, 4.94-4.97, 7.1
Real Property Exchanges (3d ed Cal CEB 2002): §§1.101, 2.66, 4.127, 4.165, 4.178, 6.93, 8.52, 15.50
Residential Environmental Hazards: A Guide For Homeowners, Homebuyers, Landlords and Tenants. California Dep't of Toxic Substances Control: §6.54
Retail Leasing: Drafting and Negotiating the Lease (Cal CEB 2007): §§1.34, 4.73, 15.39
Robinson, Gerald F. Federal Income Taxation of Real Estate. 6th ed. Boston, Warren, Gorham & Lamont, 1995: §§8.34-8.35
Robinson, W. W. Land in California. New York, Arno Press, 1979: §11.1
Russ, Lee R. Couch on Insurance. 3d ed. St. Paul, Minn., West, 1995: §13.61
Sales and Mergers of California Businesses (Cal CEB 2002): §§5.1, 5.10, 5.12, 5.14, 5.16, 5.19, 5.29, 11.118
Scott, James C. Friedman on Contracts and Conveyances of Real Property. 7th ed. New York, Practising Law Institute, 2003: §4.3
Secured Transactions in California Commercial Law Practice (2d ed Cal CEB 2001): §§4.33, 4.122, 11.118
Selecting & Forming Business Entities (2d ed Cal CEB 2007): §4.20
Shalowitz, A. L. U.S. Department of Commerce, Coast and Geodetic Survey, Shore and Sea Boundaries. 2 vols. Washington, U.S. Government Printing Office, 1962, 1964: §11.82
Smith, Jeremy D. Foreign Investment in United States Real Estate. New York, Wiley, 1992: §1.89
Uniform System of Accounts for the Lodging Industry. 10th ed. Lansing, Mich., American Hotel and Lodging Educational Institute, 2006: §5.8
Wattles, Gordon A. Writing Legal Descriptions in Conjunction With Survey Boundary Control. 4th ed. Tustin, Cal., Wattles Publications, 1981: §11.17
West Group. Restatement (Second) of Agency. Eagan, Minn., 1958: §§2.24, 2.126
————————. Restatement (Second) of Contracts. Eagan, Minn., 1981: §§3.16, 3.26, 3.30
————————. Restatement of Contracts. Eagan, Minn., 1932: §13.81
————————. Restatement (Third) of Property. Eagan, Minn., 2000: §§11.43
————————. Restatement of Property. Eagan, Minn., 1944: §§11.66-11.67, 11.108
Wielinski, Patrick J. and Jack P. Gibson. Broad Form Property Damage Coverage. 3d ed. Dallas, Tex., International Risk Management Inst., 1992: §14.60
Witkin, Bernard E. California Evidence. 4th ed. San Francisco, Bancroft-Whitney, 2000: §4.159
————————. California Procedure. 5th ed. San Francisco, Bancroft-Whitney, 2008: §§4.6, 4.154, 11.90
————————. Summary of California Law. 10th ed. San Francisco, Bancroft-Whitney, 2005: §§2.29, 2.51, 2.126, 2.186, 4.13, 4.22, 4.25, 4.67, 4.107, 4.154, 4.161, 8.21, 11.2, 11.43, 11.68, 11.80, 11.86, 13.11, 13.26
Wrongful Employment Termination Practice (2d ed Cal CEB 1997): §5.18

© The Regents of the University of California

Table of Forms

Access license and indemnity agreement, App P
Alternative form of disclosure of natural hazard conditions, App N
Assignment of intangibles, App J
Assignment of leases, App I
Bill of sale, App H
Board resolution authorizing purchase, App D
Brokerage industry
  Acknowledgment of receipt, broker's acceptance, 2.88
  Broker cooperation, submitting listing to MLS, 2.75
  Buyer's excluded from agency, 2.80
  Commission, entitlement to, 2.79
  Confirmation of agency relationship, 2.37
  Deposits
    Authority to accept, 2.68
    Handling deposits, 2.70
  Disclosure of agency relationship, 2.36
  Duties of broker, 2.84
  Escrow holder, designation of, 2.72
  Exclusive authorization to acquire property (Buyer-Broker Compensation Contract, CAR Form BBE), 2.90
  Listing period, 2.64
  Listing price, 2.66
  Nonexclusive (open) agency residential listing agreement (Authorization and Right to Sell, CAR Form RLAN), 2.60
  Possession, 2.73
  Printed form subordinate to drafted provisions, 2.87
  Residential listing agreement (Exclusive Authorization and Right to Sell, CAR Form RLA), 2.57
  Sale after termination of listing agreement (safety or protection clause), 2.82
Certification of nonforeign status by corporation, partnership, trust, or estate, 15.82
Deeds
  Compliance with obligation recitals, 10.45-10.47
  Correcting, removing, and releasing recitals, 10.42-10.44
  Deed in lieu of foreclosure, 10.41
  Execution, 10.59-10.66
  Grant deed, 10.7, App G
  Grantee recitals, 10.31-10.34
  Grantor recitals, 10.15-10.21
  Married persons conveying property, 10.39-10.40
  Reservation recitals, life estate and mineral rights, 10.51-10.52
  Separate statement of documentary transfer tax, 10.12
  Statutory form (CC §1092), 10.3
  Subordination addendum, 9.80, 9.82
  Termination recitals, 10.48-10.50
Description of property by referencing maps and other instruments, 11.100-11.102
Easements (creation, reservation, or transfer), 11.105-11.107
Escrow procedure
  Buyers/borrowers estimated closing statement, App X
  Buyer's supplemental escrow instructions, 15.50-15.61
  Consent of escrow holder, 4.180
  Escrow instructions, general provision, App S
  Foreign Investment in Real Property Tax Act (FIRPTA) certification, App W
  Letter of intent, 3.43
  Preliminary change of ownership report, App BB
  Seller's supplemental escrow instructions, 15.63-15.73
  Settlement statement, App Y
  Withholding
    Computation of estimated gain or loss (FTB Form 593-L), App T
    Real estate withholding certificate (FTB Form 593-C), App U
    Real estate withholding installment sale agreement (FTB Form 593-I), App V

Estoppel certificate from hotel operator, App R
Estoppel certificate from tenants, App K
Hotel, purchase and sale agreement for
Assets and liabilities, 5.11
Closing conditions, 5.25
Definitions, 5.9
Due diligence documents, 5.13
Employees, 5.19
Escrow and closing, 5.29
Preclosing covenants (seller), 5.15
Representations and warranties (seller), 5.17
Sample, App Q
Letter of intent, 3.33-3.46
Limited liability company certificate authorizing purchase, App E
Option agreement, 8.59-8.83
Property insurance
Assumption of risk by buyer, 13.9
Assumption of risk by seller, 13.10
Code governs except as expressly agreed, 13.13
Material loss defined, 13.5
Risk of nonmaterial loss, 13.7
Purchase and sale
Agreement of sale, 4.169
Allocation of purchase price, 4.182
Buyer's contingencies, 4.171
Closing, 4.175
Closing conditions, 4.174
Consent of escrow holder, 4.180
General provisions, 4.178
Hotel (see Hotel, purchase and sale agreement for, above)
Purchase price, 4.170
Recitals, 4.168
Remedies for default, 4.177
Representations and warranties, 4.173
Risk of loss, 4.176
Seller financing
Acceleration and default, 9.47
All-inclusive financing, 9.65
Cash downpayment, 9.40
Credit for existing encumbrances, 9.41
Partial release of lots, 9.105-9.107
Promissory note for balance, 9.45-9.46
Release on condemnation award, 9.110
Seller financing addendum and disclosure (CAR SFA), 9.13
Subordination, 9.78, 9.80-9.82, 9.87, 9.91, 9.93
Substituted security for releases, 9.109
Unencumbered conveyance at close of escrow, 9.109
Seller's preclosing covenants, 4.172
Signature, 4.179
Subordination agreement, 9.80, 9.82
Table of exhibits, 4.181
Tenant letter from owner/seller regarding rent obligation, App L
Title and introductory paragraph, 4.167
Residential purchase and sale transactions
Buyer's inspection advisory (CAR Form BIA), 6.25
California residential purchase agreement and joint escrow instructions (CAR Form RPA-CA), 6.24
Local transfer disclosure statement, 6.39
Natural hazard disclosure statement (CAR Form NHD), 6.50
Notice to buyer to perform (CAR Form NBP), 6.28
Purchase agreement addendum (CAR Form PA-A), 6.26
Real estate disclosure statement, 6.37
REO advisory (CAR Form REO), 6.111
Short sale addendum (CAR Form SSA), 6.28A
Statewide buyer and seller advisory (CAR Form SBSA), 6.27
Statement of partnership authority for general partnership, App F

Subordination addendum, 9.80, 9.82
Tenancy-in-common agreement, App O
Tenant letter from owner/seller regarding rent obligation, App L
Waiver to be executed by non-owner spouse when selling property, App M
Warranty deed covenants, 12.12

© The Regents of the University of California

Index

A B C D E F G H I J K L M N O P Q R S T U V W X Y Z

The symbol "" indicates that a form appears in the section.

Abandoned Property
Description of abandoned property, 11.62, 11.80
Doctrine of abandonment, 11.80
Easements, termination of, 11.62
Roads, reversion to fee owner, 4.58

Abatement
Hazardous substances abatement orders, 7.15

Acceleration of Payment
See also **Prepayment**
Generally, 9.47
Default, 9.47
Due-on-sale clauses. See **Due-on-Sale/Encumbrance Clauses**

Acceptance
Deeds, 10.75
Offer to buy or sell. See **Offer To Buy or Sell**
Qualified acceptance constituting counteroffer, 6.5

Access to Property
Generally, 4.90, 4.172
Easements. See **Easements**
Implied intent to dedicate, negating by showing grant of license to use, 11.77
Remediation purposes, 7.85, 7.94

Accidents. See **Liability Insurance for Real Property Transfers**

Accounts and Accounting
Attorney trust account recordkeeping, 1.12
Broker's duty to account for all funds held on client's behalf, 2.149
Consequences of transaction, 1.54
Impound accounts. See **Escrow**
Lease-option transactions, 9.21
Misappropriated funds. See **Misappropriated Funds**
Open transactions, 9.38
Prepayment restrictions, accounting year method, 9.30
Property insurance coverage for accounts receivable, 13.68

Acknowledgments
See also **Verification**
Corporate conveyances, acknowledgment required, 10.65
Defective acknowledgments
Generally, 10.1
Date of execution, effect on priority of conflicting deeds, 10.53
Effect of, 10.69
Escrow. See **Escrow**
Execution of documents. See **Execution of Documents**
Lease with option to purchase, acknowledgment as condition for recording, 10.46
Necessary element of deeds, 10.6
Notaries, 10.68, 15.89
Person not named in deed, effect of signature and acknowledgment of, 10.55
Requirements, 10.67
Spousal power of attorney, 4.19
Unacknowledged documents, 10.68, 10.70
Verification distinguished from, 10.68
Witness acknowledgment distinguished, 15.89

ACMs (Asbestos-Containing Materials). See **Hazardous Materials and Toxic Waste**

Acquired Immune Deficiency Syndrome (AIDS)
Disclosure of occupant's death from AIDS, no requirement of, 6.65

Acreage. See **Description of Property**

Acts of God or War
Contamination of property, remediation liability, 7.22

Adjacent Property
Industrial use zone, disclosures requirements if property adjacent to, 6.46

Adjoining Landowners
See also **Boundaries**
Agreed boundaries, 11.78
CC&Rs. See **Covenants, Conditions, and Restrictions (CC&Rs)**
Description by reference to, 11.29
Developer's considerations, 4.130
Easement, adjoining landowner-purchaser's considerations, 4.130
Monuments, duty to maintain, 11.36
Party walls, 4.65
Supplemented description in later deeds adding ambiguity, agreement with contiguous owners, 11.96
Water
Groundwater contamination, 7.4, 7.30-7.31, 7.37
Surface waters, strict liability for damages, 4.77

Administrative Law
Disciplinary proceedings. See **Disciplinary Proceedings**
Real Estate Commissioner. See **Real Estate Commissioner**

Administrators. See **Executors and Administrators**

Adverse Possession
Easements. See **Easements**
Elements, 11.77
Marketability of title, 4.68
Minors, 4.15
Public property, 11.57

Advertising
Broker's advertising, regulation of, 2.12
MLS. See **Multiple Listing Services (MLS)**
Party wall use, 4.65

Advertising Injury. See **Liability Insurance for Real Property Transfers**

Affidavits and Declarations
CC&Rs. See **Covenants, Conditions, and Restrictions (CC&Rs)**
Homestead declarations. See **Homestead Property**
Joint tenant's death, recording affidavit, 4.19
Segregating taxes when part of assessed parcel sold, 4.133
Streets and passageways, filing map as declaration of right to use, 11.24
Title insurer, seller's affidavit providing information for, 15.40
Withholding exemption, seller's declaration concerning, 15.77

After-Acquired Title. See **Deeds**

Age Discrimination. See **Senior Citizens**

Agents and Agency
Authority to sign, writing aspect, 4.12
Brokerage industry. See **Brokers, Dealers, and Real Estate Salespersons**
Buyer's use of agents or nominees. See **Purchase and Sale Agreement**
Contaminated property
Environmental consultant, principal-agent considerations, 7.44
Liability, third party defense, 7.23
Corporate agent binding corporation, 4.28, 4.156
Escrow. See **Escrow**
Knowledge of agent imputed to seller, 6.30
Liability insurance for. See **Liability Insurance for Real Property Transfers**

Partnership, agent's signature binding on, 4.156
Power of attorney. See **Attorneys**
Question of fact, agency's existence as, 4.5
Recorder as agent of grantee or mortgagee, 15.92
Underwritten title companies as agents for title insurers, 15.15

Agreements. See **Contracts**

Agricultural Property
Agricultural Foreign Investment Survey Act, reporting requirements under, 1.89
Contamination by pesticides and fertilizers, 7.3
Crops sale, writing unneeded, 4.13
Sale subject to lease, 4.74
Tax treatment
Federal estate taxes, 4.62
Williamson Act tax incentives, 1.86, 4.93

Airports
Disclosure requirements if property located near airport, 6.46

Air Quality
Pollutants, land use regulations, 7.7

All-Inclusive Instruments (Wraparound Financing). See **Mortgages and Trust Deeds**

Allocation
Contaminated property, allocation of remediation or removal costs. See **Hazardous Materials and Toxic Waste**
Escrow. See **Escrow**
Purchase price, allocation of, 4.36, 4.182

ALTA. See **American Land Title Association (ALTA)**

Alternative Dispute Resolution (ADR)
See also **Arbitration; Mediation**
Purchase and sale agreement provision, 4.150, 4.177
Residential purchase and sale transactions. See **Residential Purchase and Sale Transactions**

Alternatives to Sale
Generally, 1.26
Purchaser's alternatives
Generally, 1.33
Equity transactions, 1.35
Leasing transaction, 1.34
Nonpursuit of transaction, 1.36
Seller's alternatives
Development of property in furtherance of sale, 1.31
Goals and liquidity sources, 1.24, 1.28-1.30, 1.32
Leasing transaction, 1.27

Ambiguity
Damages for breach despite ambiguity, 11.15
Deeds, ambiguities in, 11.15, 11.25, 11.96
Description of property, 11.15-11.16, 11.97
Easement description, 11.70
Escrow instructions. See **Escrow**
Extrinsic evidence, interpreting, 4.159, 11.15
Grant by public agency, interpretation of ambiguity in favor of public agency, 11.15
Mutual asset to contract, effect of ambiguous language on, 4.8

Amendments and Modifications
Easement, amendment of written descriptions by actual location, 11.48
Escrow instructions, modification or revocation of, 15.18, 15.30
Integration clause, 4.159
Listing agreement, oral modification of, 2.53
Purchase and sale agreement. See **Purchase and Sale Agreement**
Writing requirement, 4.158-4.159, 4.178
Zoning ordinance amendments, 4.86

American Land Title Association (ALTA)
ALTA and CLTA policies distinguished
Generally, 1.134
Description of property, 11.11-11.12

Extended ALTA coverage, 4.57, 4.134
Survey endorsement to ALTA policy, 11.75

Annexation of Property, 4.91

Antideficiency Protection, 4.41, 9.1, 9.8-9.9, 9.55, 9.95-9.99

Antitrust Laws
Brokers' agreement setting commission rates as violation of, 2.118

Appraisals and Appraisers
See also **Valuation of Property**
Property insurance dispute, arbitration versus appraisal to resolve, 13.97
Reappraisal, triggering events, App A
Right to receive copy of appraisal report, 9.12

Arbitration
See also **Alternative Dispute Resolution (ADR); Mediation**
Generally, 4.150, 4.177
Brokers, arbitration of claims against
Generally, 2.154
National Association of REALTORS' code of ethics requiring members to arbitrate with each other, 2.175
Pre-litigation and pre-arbitration duty to mediate, 2.153A
Federal Arbitration Act, preemption of state law by, 6.15, 6.18-6.18A
Listing agreement, arbitration clause in, 2.85
Property insurance dispute, arbitration versus appraisal to resolve, 13.97
Purchase and sale agreement clause, 4.150, 4.177
Remediation disputes, 7.84
Residential purchase transactions. See **Residential Purchase and Sale Transactions**

Architects
Certificate of completion, 4.105
Liability insurance for, 14.6

Arson
Property insurance, effect of insured's act of arson on coinsured's claim, 13.30

Articles of Organization
Limited liability company, 4.27

Asbestos-Containing Materials (ACMs). See **Hazardous Materials and Toxic Waste**

As-Is Clause
Purchase and sale agreement, 4.49, 4.120, 4.173, 6.9, 7.64, 7.65
Seller's failure to disclose known or hidden defects, effect of "as is" clause on, 2.185
Toxic contamination, 7.64, 7.65

Assessments. See **Taxes and Tax Assessments**

Assignment
Generally, 4.155
Agreement binding on successors, 4.161, 4.178
Contracts. See **Contracts**
Covenants of title, 12.8, 12.20
Easements in gross, 11.69
Escrow. See **Escrow**
Impound account on loan, buyer assumes, 4.133
Intangibles, assignment agreement, App J
Leases, 4.73, 4.75, 8.57, App I
Membership agreements in resort facilities, assignment to buyer of hotel, 5.6
Option contract for purchase of real property, assignability of, 8.25, 8.70
Party to escrow assigning proceeds, enforceability by broker against escrow holder, 15.14
Property insurance policy, assignment of, 13.24
Purchase agreement, 4.73, 4.75, 4.155-4.157
Remediation rights, 7.92

Assumption of Risk. See **Risk of Loss**

Attachment
Federal tax lien hearing, 4.62

Attorney-Client Relationship

Areas to be explored with client
Alternatives to sale. See **Alternatives to Sale**
Experts and specialists. See **Experts**
Knowledge and experience of seller and purchaser, 1.55-1.56
Net proceeds requirements. See **Net Proceeds Requirements**
Purpose and objectives in selling or buying property, 1.23-1.25
Risk tolerance. See **Risk (Generally)**
Timing needs. See **Time**
Commingling of attorney's and client's fund prohibited, 1.12
Conflict of interest. See **Conflict of Interest**
Consent. See **Consent**
Contaminated property transactions, attorney's role, 1.57, 1.64, 7.1, 7.71
Fees. See **Attorneys' Fees**
Fiduciary relationship. See **Fiduciary Relationship**
Financial objectives, consequences of transaction, 1.54
Leases, attorney's review of, 4.71-4.72
Malpractice. See **Legal Malpractice**
Marketing property. See **Marketing Property**
Needs and objectives as important guideposts, 1.22
Piecemeal involvement of attorney, consequences of, 1.18
Professional liability insurance, disclosure requirements for, 1.12A
Receipt of client's funds or property, notifying client of, 1.12
Role in conveyance transaction
Description of property, 11.3-11.8
Documents prepared by others, reviewing, 4.5
Due diligence. See **Due Diligence**
Escrow. See **Escrow**
Leases, examination, 4.73, 4.75
Liquidated damages clauses, review enforceability of, 1.99
Negotiation. See **Negotiation**
Structuring transaction (see Structuring transaction, below)
Title insurance preliminary report, reviewing exceptions, 4.54
Zoning considerations, 4.86, 4.113
Scope of services provided, 1.17
Structuring transaction
Generally, 1.94, 1.97
Closing process. See **Escrow**
Duty to review printed forms, 4.5
Financing, 9.2-9.5
Flexibility of client, 1.103
Forms of transaction, reviewing, 1.98
Legal opinions, drafting. See **Legal Opinions**
Letter of intent for seller, 1.102
Preparation of transactional documents, 1.119-1.120
Seller or purchaser entities, considerations on, 1.95-1.96
Tax-deferred exchange, 1.101
Warranties, review strategies concerning, 1.100
Tax advice, 1.20

Attorney General
Unruh Civil Rights Act, enforcement of, 6.101

Attorneys
Generally, 1.1-1.2
Arranger of credit exception, 9.10
Attorney-in-fact. See **Power of Attorney**
Client relationship. See **Attorney-Client Relationship**
Conflict of interest. See **Conflict of Interest**
Description of property responsibilities, 11.3-11.8
Disciplinary proceedings. See **Disciplinary Proceedings**
Escrow. See **Escrow**
Ethics. See **Legal Ethics**
Fees. See **Attorneys' Fees**
Financing, attorney's role and standards of care, 9.2-9.5
Foreclosure or probate sale, attorney's purchase of property prohibited, 1.7
Malpractice. See **Legal Malpractice**
Notice
Postclosing follow-up by attorney, monitoring notices and actions, 1.144
Receipt of client's funds or property, notice to client of, 1.12
Opinions. See **Legal Opinions**
Power of attorney. See **Power of Attorney**
Privilege, 1.64

Purchase and sale agreement, attorney's role in negotiating, 1.116, 1.118
Residential transactions, attorney's role in, 6.2
Title insurance. See **Title Insurance and Preliminary Report**

Attorneys' Fees
Agreement
Generally, 1.19
Amount of fee, 1.20
Equity interests, 1.21
Broker's breach of fiduciary duties, recovery of fees in action based on, 2.158
California Land Use & Revitalization Act, recovery of attorney fees under, 7.32
Contaminated property. See **Hazardous Materials and Toxic Waste**
Covenants of title breach, 12.15, 12.18
Escrow. See **Escrow**
Experts compensation, 1.57
Fair Housing Act (FHA), recovery of fees under, 6.100
Home equity sale contract, recovery of fees by seller, 6.109
Indemnity agreement providing for attorney fees, 7.66
Option contract, provision covering attorney fees, 8.76
Prohibition against accepting compensation for representing other clients, 1.10
Property insurance, recovery of fees in action for breach of, 13.115
Purchase and sale agreement clause, 4.142, 4.153, 4.178
Residential purchase and sale agreement, provision for attorney fees, 6.19

Bad Faith. See **Good Faith and Fair Dealing**

Balloon Payments
See also **Financing**
Computation of payments, 9.44
Seller financing, 9.11

Bankruptcy and Insolvency
Acceleration of payment, seller declaring default if buyer files bankruptcy, 9.47
Attorney's opinion regarding formation of buyer, 9.3
Automatic stay, effect on guarantor or co-obligor of note, 9.47
Deceased joint tenant's property, 4.22
Option contract for purchase of real property, effect of optionor filing bankruptcy petition on, 8.28
Recovery Account of Real Estate Fund, requirement claimant represent that underlying judgment and debt not discharged in bankruptcy, 2.168
Seller's alternatives, seeking protection of bankruptcy proceeding, 1.32

Banks and Banking
Escrow law, exemption of banks from, 15.6

Bars on Windows. See **Window Security Bars**

Basis
Mortgage exceeding basis at time of sale, 9.28-9.29
Option payments added to basis of property, 8.36
Surviving spouse, step-up in basis limited to, 6.91

Bids and Bidding
Marketing property, negotiated or bidding sale considerations, 1.106-1.107, 1.111-1.112
Private bidding sale, considerations on using, 1.107

Bill of Sale
Personal property transferred with real property, 11.97
Sample, App H

Bona Fide Purchasers
Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA), bona fide prospective purchaser defense under, 7.22, 7.31, 7.34
Defects in title, inspection of property to support bona fide purchase defense, 11.75
Easements by implication, 11.54
Quitclaim deeds, protections for grantee of, 10.4
Recording Act, 12.2
Third parties dealing with trustees, 10.47

Bonds and Undertakings
Attorney negligently drafting bond indenture, 9.5
Buyer's assumption of existing debt, seller becoming surety by, 4.41

Guaranty
Automatic stay in bankruptcy, effect on guarantor of note, 9.47
Remediation costs payment security, 7.82
Performance bond securing buyer's obligations, 4.78
Subordination agreements. See **Subordination**

Boundaries
See also **Adjoining Landowners**
Agreed boundaries doctrine, 11.78
Declaratory relief in boundary dispute action, 11.90
Estoppel, effect on boundaries, 11.88
Inspection of residential property for evidence of possible boundary disputes, 6.7
Metes and bounds description using adjoining lands, 11.29
Practical location doctrine, 11.79
Seller's knowledge and notice of boundaries, 4.59
Tidal and submerged lands, 11.82
Water, effect on boundaries, 11.81-11.86, 11.110

Breach of Contract
See also **Contracts**
Brokers. See **Brokers, Dealers, and Real Estate Salespersons**
Consideration insufficient or lacking, 4.11
Description of property, damages for breach despite ambiguity, 11.15
Measure of damages in breach of contract action, 2.156, 15.22
Property insurance. See **Property Insurance**
Statute of limitations, 15.22
Termination of contract based on, 4.164

Breach of Covenant
Escrow. See **Escrow**
Title. See **Covenants of Title**

Brokers, Dealers, and Real Estate Salespersons
See also **Listing Agreement; Multiple Listing Services (MLS)**
Generally, 2.1
Advertising by broker, regulation of, 2.12
Agency relationships
Broker acting in non-agency capacity, 2.38A
Changing agency elections, 2.34
Confirmation of agency relationship, 2.37
Conflict of interest (see Conflict of interest, below)
Contract law versus agency law, 2.26
Creation of agency (see Creation of agency without written contract, below)
Disclosure (see Disclosure, below)
Dual agency (see Dual agency of listing agents, below)
Escrow agent, broker as. See **Escrow**
Fiduciary duty of broker arising at creation of agency relationship, 2.125
Listing agreements. See **Listing Agreement**
Measure of damages in agency situations, 2.159
Options regarding, 2.33-2.34
Salesperson as agent of broker, 2.20
Statute of frauds, agency relationship with seller not subject to, 2.125
Arbitration. See **Arbitration**
Breach of contract
Buyer's breach, broker's right to deposit or damages, 2.119
Measure of damages, 2.156
Punitive damages for breach, unavailability of, 2.162
Seller's breach or inability to perform, effect on broker's recover of commission, 2.108
Third party, broker's liability to, 2.180
Breach of fiduciary duty, claims against broker for
Generally, 2.152
Arbitration of claims against broker, 2.154
Attorney fees, recovery of, 2.158
Bases of liability for broker's breach of fiduciary duty, 2.153
Breach of contract actions, measure of damages in, 2.156
Commission, client's recovery of, 2.161
Common law, recovery of damages under, 2.153
Fraud cases, limits on recovery in, 2.156
Multiple listing service (MLS), breach of fiduciary duty to persuade seller to keep listing out of, 2.74
Pre-litigation and pre-arbitration duty to mediate, 2.153A
Standards for awarding damages, 2.155
Statute of limitations for action based on broker's breach of duty to disclose, 2.183

Tort measure of damages, 2.158
Burden of proof. See **Burden of Proof**
Buyer, recovery of commission from
Implied covenant for buyer's completion of purchase, 2.120
Interference with prospective economic advantage (see Interference with prospective economic advantage as grounds for broker's recovery of commission from buyer, below)
Claims against broker
Damages, recovery of (see Damages, below)
Fiduciary duty, breach of (see Breach of fiduciary duty, claims against broker for, above)
Recovery Account (see Recovery Account of Real Estate Fund, recovery of unsatisfied judgments from, below)
Secret profits, recovery from broker, 2.160
Commissions and compensation
Generally, 2.91
Amount of commission, 2.118
Antitrust laws, brokers' agreement fixing commission rates as violation of, 2.118
Breach of contract by buyer, broker's right to deposit or damages, 2.119
Breach of fiduciary duty as grounds for client's recovery of commission, 2.161
Buyer (see Buyer, recovery of commission from, above)
Buyer-broker agreements, 2.89, 2.90
Closing, avoiding claims for commissions or finder's fees after, 4.135
Conditional purchase agreement, effect of buyer and seller executing, 2.108
Conditions. See **Listing Agreement**
Cooperating broker (see Cooperating (buyer's) broker, compensation of, below)
Escrow. See **Escrow**
Estoppel theory, broker's inability to collect commission based on, 2.51
Exclusive right-to-sell agreement without definite termination date, disciplinary action against broker trying to recover compensation under, 2.56
Lack of diligence as defense in action for payment of commission, 2.148
Letter of intent, 3.44
License as prerequisite for recovering commission, 2.91, 2.94
Listing agreement provisions concerning. See **Listing Agreement**
Option contract, broker's commission on, 8.74
Option for sale of property, broker receiving commission on exercise of, 2.98
Partnership or joint venture, broker receiving commission if property conveyed to, 2.98
Probate sales, commission payment regulations, 1.106
Procurement of sale requirement (see Procuring cause of sale, broker as, below)
Ready, willing, and able buyer requirement (see Ready, willing, and able buyer, below)
Referral fees and fee-splitting arrangements, restrictions on, 2.5, 2.135
Secret (see Secret profits, below)
Self-representation by buyer-broker, recovery of commission prohibited, 2.96
Statute of frauds. See **Statute of Frauds**
Transaction other than outright sale, broker's right to commission following, 2.98
Withdrawal of seller from sale (see Withdrawal of seller from sale, broker's right to compensation, below)
Common law. See **Common Law**
Conflict of interest
Generally, 2.128
Dual agency, disclosure of, 2.129
Other multiple agency scenarios, 2.130
Self-dealing by broker (see Self-dealing by broker, below)
Contractual relationships
Essential elements of contract, 2.43
Execution of broker's contract, 2.47
Listing agreement. See **Listing Agreement**
Statute of frauds. See **Statute of Frauds**
Cooperating (buyer's) broker, compensation of
Breach of contract by buyer, cooperating broker's right to full commission from buyer, 2.119
Procuring cause of sale, cooperating broker's recovery from listing broker, 2.104
Requirements for recovery of commission by cooperating broker, 2.93
Seller's withdrawal from sale or refusal to close, cooperating broker's remedies for, 2.108
Creation of agency without written contract
Generally, 2.27
Express or implied agreement, agency by, 2.28
Ostensible agency, creation of, 2.30
Ratification of previously unauthorized actions, creation of agency by, 2.29
Criminal penalties (see Penalties, below)
Damages
Breach of contract by buyer, broker's right to deposit or damages, 2.119
Breach of fiduciary duty (see Breach of fiduciary duty, claims against broker for, above)
Indemnification from broker for damages recovered by third parties because of broker's actions, 2.163
Negligent actions of broker, measure of damages for, 2.159
Punitive damages, 2.162
Unreasonable delay or negligence, broker's liability for damages suffered by client based on, 2.142, 2.159

Dealer property, 9.32
Definitions of brokerage industry terminology. See **Definitions**
Delivery of documents. See **Delivery of Documents**
Deposits. See **Deposits**
Description of property, limited duties of inspection and disclosure, 11.11
Disciplinary proceedings
  Accusation filed by Real Estate Commissioner, 2.173
  Authority of Real Estate Commissioner to bring disciplinary action against brokers and salespersons, 2.171
  Corporation, disciplinary action against for individual corporate broker's violation of Real Estate Law, 2.4
  Exclusive right-to-sell agreement without definite termination date, disciplinary action against broker trying to recover compensation under, 2.56
  Grounds for, 2.171
  Hearings (see Hearings, below)
  Local association of REALTORS proceedings, 2.175
  Mitigating factors, 2.172
  Multiple listing services (MLS), disciplinary action against, 2.175
  Overstating value of property to obtain listing, disciplinary action against broker for, 2.65
  Penalties (see Penalties, below)
  Real Estate Commissioner proceedings, 2.171-2.174
  Remedies, 2.174
  Statute of limitations for, 2.173
Disclosure
  Generally, 2.127
  Accuracy of disclosures by seller or seller's broker, no duty on buyer's broker to verify, 2.127
  "As is" provision, effect on seller's liability for broker's failure to disclose defects, 2.185
  Conflict of interest, disclosure of (see Conflict of interest, above)
  Description of property, limited duties of inspection and disclosure, 11.11
  Dishonest client instructing broker not to disclose material information, 2.136
  Distinguishing statement intended to encourage negotiations from disclosure of confidential information, 2.139
  Dual agency, disclosure of, 2.129
  Form, disclosure of agency relationship, 2.36
  Mortgage loan brokers, disclosure requirements and limits on charges, 2.8
  Net listing arrangement, broker's disclosure to seller of fees received under, 2.61
  Nontraditional and subprime mortgage products, disclosure and compliance requirements for, 2.8A
  Price and value (see Price and value, broker's advice on, below)
  Principal, broker's liability for failure to disclose, 2.186
  Relative, employee, or entity in which broker has interest, disclosure of purchase by, 2.133
  Resale of manufactured home, disclosures in, 6.35
  Residential loan modifications, disclosure requirements for, 2.8B
  Secret profits or other benefits obtained in transaction, broker's liability to principal for, 2.135
  Self-dealing by broker (see Self-dealing by broker, below)
  Third parties (see Third parties, broker's liability to, below)
Disclosure of agency relationships in residential and lease transactions
  Generally, 2.31
  Failure to disclose agency relationship, lack of penalties for, 2.32
Dual agency of listing agents
  Generally, 2.35
  Buyer-broker agreements, 2.89, 2.90
  Consent to, 2.130
  Disclosure requirements, 2.129
  Unintended dual agency, 2.38
Due diligence. See **Due Diligence**
Duties broker owes principal
  Account, duty to, 2.149
  Accuracy of other's representations, no duty to verify, 2.150
  Area of expertise, no duty to advise client on matters outside, 2.151
  Disclosure (see Disclosure, above)
  Due diligence, broker's lack of as grounds for revoking listing, 2.83, 2.148
  Exercise of reasonable skill and care (see Reasonable care, broker's duty to exercise, below)
  Fiduciary (see Fiduciary duties, below)
  Listing agreement provisions concerning. See **Listing Agreement**
Errors and omissions insurance for real estate agents
  Generally, 14.72
  Claims made basis, coverage on, 14.73
  Exclusions, 14.75
  Representative insuring clause, 14.74
Escrow. See **Escrow**
Estoppel. See **Estoppel Doctrine**
Ethics (see Disciplinary proceedings, above)
Exclusive right to sell. See **Listing Agreement**
Exemptions from licensing requirements
  Generally, 2.6

Finders, exemption for, 2.5
Mortgage loan brokers (see Mortgage loan brokers, below)
Fiduciary duties
Agency relationship, broker's fiduciary duties arising at creation of, 2.125
Breach of (see Breach of fiduciary duty, claims against broker for, above)
Disclosure (see Disclosure, above)
Due diligence, broker's lack of as grounds for revoking listing, 2.83, 2.148
Enforceable contract claim for commission, fiduciary duties of broker despite lack of, 2.26
Post-closing obligations related to sale, fiduciary duties including, 2.126
Price and value (see Price and value, broker's advice on, below)
Reasonable care (see Reasonable care, broker's duty to exercise, below)
Standard of care, 2.124, 2.142
Statute of limitations. See **Statutes of Limitations**
Third parties, lack of fiduciary duty to, 2.176
Financing. See **Financing**
Finders
Closing, avoiding claims for commissions or finder's fees after, 4.135
Distinguished from brokers, 2.5
Misrepresentation by principal, finder's recovery based on, 2.50
Statute of frauds, finder invoking doctrine of estoppel to overcome, 2.51
Fraud and misrepresentation
Disciplinary proceedings for (see Disciplinary proceedings, above)
Measure of damages for fraud or misrepresentation, 2.156-2.158
Principal's liability for broker's misrepresentations and nondisclosure, 2.184
Principal's misrepresentations, broker's recovery for fraud based on, 2.50
Recovery Account of Real Estate Fund, recovery of unsatisfied judgment for fraud or misrepresentation from, 2.164, 2.166-2.167
Salesperson's fraud, misrepresentation, or deceit, broker's liability for, 2.15
Third parties, broker's liability for misrepresentations (Third parties, broker's liability to, below)
Third parties, principal's liability for broker's actions (see Third parties, principal's liability for broker's actions, below)
Hearings
Desist and refrain order, broker's right to administrative hearing on, 2.174
Revocation or suspension of license, hearing on, 2.173
Indemnity. See **Indemnity**
Insurance
Errors and omissions insurance (see Errors and omissions insurance for real estate agents, above)
Unemployment insurance system, exclusion of brokers and real estate salespersons from, 2.17
Interference with prospective economic advantage as grounds for broker's recovery of commission from buyer
Generally, 2.121
Burden of proof, 2.123
Elements of cause of action, 2.122
Interpretive opinions, 2.12A
Judgments against licensees (see Recovery Account of Real Estate Fund, recovery of unsatisfied judgments from, below)
Kickbacks prohibited, 2.135
Licensing
Generally, 2.2
Commission, license as prerequisite for recovering, 2.91, 2.94
Corporations and partners as licensees, 2.4
Escrow agent, license requirements for broker acting as, 2.22
Exemptions (see Exemptions from licensing requirements, above)
Mortgage loan brokers, 2.7
Qualifications for licensing, 2.3
Revocation of license (see Revocation or suspension of license, below)
Specialized licensees (see Specialized licensees, below)
Listing agreement. See **Listing Agreement**
Malpractice insurance (see Errors and omissions insurance for real estate agents, above)
Misrepresentations (see Fraud and misrepresentation, above)
Mortgage loan brokers
Generally, 2.7
Disclosure requirements and limits on charges, 2.8
Exemption from usury for loans made or arranged by, 2.9
Licensing requirements, 2.7
Nontraditional and subprime mortgage products, disclosure and compliance requirements for, 2.8A
Residential loan modifications, disclosure requirements for, 2.8B
Negligence
Measure of damages for broker's negligence, 2.159
Third party, broker's liability for negligence affecting, 2.179
Unreasonable delay or negligence, broker's liability for damages suffered by client based on, 2.142, 2.159
Offers
Communicating offers to seller, 2.141
Ready, willing, and able buyer (see Ready, willing, and able buyer, below)
Options (see Commissions and compensation, above)

Penalties
Agency relationship, no penalties for broker's failure to disclose, 2.32
Anti-money-laundering laws, penalties for violation of, 2.182
Commingling client's funds with personal funds, revocation of license for, 2.149
Criminal penalties for kickbacks, 2.135
Criminal sanctions for actions by real estate licensees, 2.174
Dual agency, denial of commission for failure to disclose, 2.129
Residential loan modifications, penalties for noncompliance with rules governing, 2.8B
Revocation of license (see Revocation or suspension of license, below)
Supervision of salesperson, penalties for broker's failure regarding, 2.15
Price and value, Overstating value of property to obtain listing, disciplinary action against broker for, 2.65
Price and value, broker's advice on
Generally, 2.137
Best price obtainable, advising seller on, 2.138
Communicating offers to seller, 2.141
Distinguishing statement intended to encourage negotiations from disclosure of confidential information, 2.139
Speculative purchases and resales, broker's liability for, 2.140
Procuring cause of sale, broker as
Generally, 2.92
Completion of sale, 2.102
Cooperating broker's recovery from listing broker, 2.104
Defined, 2.99
Introduction of parties, 2.100
Ready, willing, and able buyer requirement (see Ready, willing, and able buyer, below)
Safety or protection clause, 2.105
Showing property, 2.101
Type of listing agreement, broker's burden of proof depending on, 2.103
Profits (see Secret profits, below)
Questions of law and fact. See **Questions of Law and Fact**
Ready, willing, and able buyer
Generally, 2.106
Listing agreement requiring broker to procure, 2.92
Nonconforming or conditional offer, seller's acceptance of, 2.109
Offer accepted, effect of seller's breach or inability to perform, 2.108
Offer rejected by seller, broker's entitlement to commission, 2.107
Reasonable care, broker's duty to exercise
Generally, 2.142
Financial soundness of other party, broker's liability for advising client on, 2.143
Legal advice, 2.147
Real estate matters, advising client on, 2.145
Short sales, advice on, 2.147A
Tax considerations, advising client on, 2.146
Title matters, broker's breach of duty of care in failing to advise client to investigate, 2.144
Recovery Account of Real Estate Fund, recovery of unsatisfied judgments from
Generally, 2.164
Amounts recoverable, 2.169
Bankruptcy, claimant required to represent that underlying judgment and debt not discharged in, 2.168
Grounds for recovery, 2.166
Licensed defendant, recovery against, 2.165
Monetary penalty in lieu of suspension of license, deposit of money in Recovery Account, 2.174
Procedures for applying for payment of claim, 2.170
Reimbursement of fund by broker or salesperson, 2.170
Requirements for recovery, 2.165-2.168
Specified categories of actions, recovery allowed for, 2.167
Relationship between brokers and salespersons
Agents of brokers, salespersons as, 2.20
Bus & P C §10032, relationship between broker and salesperson under, 2.15
Common law and statutory schemes, relationship between broker and salesperson under, 2.16
Disciplinary proceedings (see Disciplinary proceedings, above)
Documenting relationship between broker and salesperson, 2.21
Exclusive representation of buyer by salesperson prohibited, 2.33
Indemnification of salesperson, 2.20
Independent contractor of employee, salesperson as, 2.15-2.16, 2.19
Licensing and employment requirements for salespersons, 2.13
Negligence of salespersons, broker's liability for, 2.179
Recovery Account of Real Estate Fund, limits on recovery for injuries inflicted by salesperson, 2.167
Supervision of salespersons, 2.14-2.20
Tort liability of broker for actions by salespersons, 2.20
Unemployment insurance, exclusion of brokers and salespersons from coverage, 2.17
Withholding income and social security taxes, 2.19
Workers' compensation, applicability to salespersons, 2.18
Resales

Disclosures in resale of manufactured home, 6.35
Speculative purchases and resales, broker's liability for, 2.140
Residential sales, disclosure requirements in (see Disclosure of agency relationships in residential and lease transactions, above)
Revocation or suspension of license
Commingling of client's funds with personal funds as grounds for, 2.149
Failure of broker to supervise salesperson resulting in loss of license, 2.15
Hearing required for, 2.173
Monetary penalty in lieu of suspension of license, 2.174
Recovery Account of Real Estate Fund, suspension of broker's license pending reimbursement of, 2.170
Salespersons, licensing and employment requirements for, 2.13
Secret profits
Generally, 2.135
Recovery from broker, 2.160
Third parties, broker's liability to, 2.177
Selection of broker, factors to consider in, 2.25
Self-dealing by broker
Generally, 2.131
Interest in property sold to client, broker's disclosure of, 2.134
Purchase of client's property, broker's disclosure requirements, 2.132
Services offered by broker, types of, 2.24
Specialized licensees
Business opportunity brokers, licensing requirements for, 2.10
Mortgage loan brokers (see Mortgage loan brokers, above)
Real estate syndicate securities dealers, 2.11
Standard form purchase contracts, real estate licensees completing, 6.2
Statute governing brokers, 2.1
Statute of frauds. See **Statute of Frauds**
Statute of limitations. See **Statutes of Limitations**
Suspension of license (see Revocation or suspension of license, above)
Taxes
Advising client on tax considerations, 2.146
Withholding income and social security taxes, 2.19
Third parties, broker's liability to
Generally, 2.176
Anti-money-laundering programs, brokers and real estate attorneys required to establish, 2.182
Breach of contract, broker's liability for, 2.180
Housing discrimination, broker's liability for, 2.181
Indemnification of broker from seller for seller's misrepresentations, 2.183
Joint and several liability of broker and seller for broker's misrepresentations to buyer, 2.183
Negligent acts or services, broker's liability for, 2.179
Nondisclosure or misrepresentation of material facts, liability for, 2.178
Secret profits received through fraud or misrepresentation, liability to third parties for, 2.177
Statute of limitations for actions by third parties against brokers, 2.178
Third parties, principal's liability for broker's actions
"As is" provision, effect on seller's failure to disclose known or hidden defects, 2.185
Indemnification from broker for damages recovered by third parties because of broker's actions, 2.163
Misrepresentations and nondisclosure by broker, principal's liability for, 2.184
Principal, broker's liability for failure regarding disclosure of, 2.186
Subsequent purchasers of property, seller's liability to third parties for fraudulent misconduct extending to, 2.187
Tort liability. See **Tort Liability**
Usury limitations, exemption for loans made or arranged by brokers, 2.9
Value (see Price and value, broker's advice on, above)
Withdrawal of seller from sale, broker's right to compensation
Cooperating broker's remedies for seller's withdrawal, 2.108
Enforceability of withdrawal-from-sale clauses, 2.114

Brownfields. See **Hazardous Materials and Toxic Waste**

Building Codes
Building permit, rights vested, 4.86, 4.89
Common law duty to disclose building code violations, 6.31A
Compliance with building code, determination of, 1.78
Engineering studies and reports, 4.77
Green building standards and requirements, 1.78
Liability insurance, responsibility for code-mandated repairs, 13.107

Bulk Sales
Hotel purchase and sale agreement complying with bulk sales laws, 5.23

Burden of Proof
See also **Evidence; Proof**

Broker transactions
Interference with prospective economic advantage, broker's burden of proving in action against buyer for, 2.123
Procuring cause of sale, broker's burden of proof depending on type of listing agreement, 2.103
Contaminated property, proving cause after close of escrow, 7.72
Conveyance subject to restrictions on use imposed as part of common interest subdivision, burden of proof on party attacking reasonableness of, 10.2
Federal Arbitration Act, burden of proof on party claiming preemption of state arbitration laws in cases involving commerce, 6.18
Property insurance. See **Property Insurance**
Recovery Account of Real Estate Fund, applicant's burden of proof in action for claim against, 2.166
Surface water runoff damages, 4.77

Business Interruption Coverage. See **Property Insurance**

Business Operations on Property
Purchase transaction. See **Purchase and Sale Agreement**
Tax treatment of rent under lease-option, 9.21
Tenancy-in-common agreement, App O

California Association of Realtors (CAR)
Escrow instructions. See **Escrow Instructions**
Listing agreement, forms for. See **Listing Agreement**
Residential purchase agreement. See **Residential Purchase and Sale Transactions**

California Coordinate System
Description of property, 11.18, 11.22

California Environmental Quality Act (CEQA). See **Hazardous Materials and Toxic Waste**

California Land Title Association (CLTA)
ALTA and CLTA policies distinguished
Generally, 1.134
Description of property, 11.11-11.12

California Land Use & Revitalization Act. See **Hazardous Materials and Toxic Waste**

Cancellation of Transactions. See **Termination of Transaction**

Capacity To Contract. See **Contracts**

Capital Gains. See **Gain or Loss**

Carpenter-Presley-Tanner Hazardous Substance Account Act (HSA). See **Hazardous Materials and Toxic Waste**

CC&Rs. See **Covenants, Conditions, and Restrictions (CC&Rs)**

CEQA. See **Hazardous Materials and Toxic Waste**

CERCLA. See **Hazardous Materials and Toxic Waste**

Certificates and Certification
Architect's certificate of completion, 4.105
Corporations. See **Corporations**
Escrow. See **Escrow**
Estoppel certificate. See **Estoppel Certificate**
Good standing certificate, 4.20
Insurance, certificate of. See **Insurance**
Limited partnership certificate, 4.19, 4.25
Nonattachment of federal tax lien, 4.62
Occupancy, Certificate of, 4.105
Partnerships. See **Partnerships**
Purchase, certificate authorizing. See **Purchase and Sale Agreement**
Recorded document, recording certified copy of, 15.90
Subdivision Map Act compliance, 4.92, 4.114
Trust, certificate of nonforeign status by, 15.82
Withholding Certificate for Disposition by Foreign Persons of U.S. Real Property Interests, seller's submission of application for, 15.83

Change of Ownership
See also **Exchange of Property**
Joint tenancy termination as change of ownership, 4.22
New base year value for assessing property taxes, 1.96

Reappraisal triggering events, App A
Transfers not qualifying as, 1.96

Charts, Checklists, Questionnaires, and Tables
Covenants of title, statute of limitations table, 12.21
Due diligence checklists. See **Due Diligence**
Listing agreement checklist, 2.55
Reappraisal triggering events, App A

Checks
Broker's receipt of deposit check, regulations affecting, 2.149
Buyer's deposit, 4.35-4.37, 4.170

Children
See also **Minors**
Family day care home for children, effect of restrictions on use or occupancy of real property on, 6.104

Chinese Drywall Claims. See **Property Insurance**

Cities and Counties. See **Local Government**

Civil Rights
Prisoners, civil rights of, 4.18
Unruh Civil Rights Act. See **Unruh Civil Rights Act**

Claims Made Policies. See **Liability Insurance for Real Property Transfers**

Cleaning Up Hazardous Materials. See **Hazardous Materials and Toxic Waste**

Closely Held Business
Federal estate tax lien, 4.62

Closing Costs
Generally, 4.134, 4.175
Buyer's deposit, 4.35-4.37, 4.170
Estimated closing statement, 15.54, App X
Estimate of closing costs, escrow agent providing to buyer and seller, 6.23
Segregated parcels, 4.133
Supplemental escrow instructions allocating, 15.42
Title insurance, 1.139, 4.56, 4.122, 4.134

Closing Escrow. See **Escrow**

CLTA. See **California Land Title Association (CLTA)**

Coastal Zone Property
California Coastal Act requirements, 1.86, 4.88

Code-Mandated Repairs. See **Building Codes**

Commercial General Liability (CGL) Insurance. See **Liability Insurance for Real Property Transfers**

Commercial Property Insurance. See **Property Insurance**

Commingling of Funds
See also **Misappropriated Funds**
Attorney's and client's funds, commingling prohibited, 1.12
Broker prohibited from commingling client's funds with personal funds, 2.149
Escrow holder's rights concerning, 15.36

Commissioner of Corporations
Escrow law, Commissioner's enforcement of, 15.4

Commission of Broker. See **Brokers, Dealers, and Real Estate Salespersons**

Common Interest Developments
See also **Residential Stock Cooperatives**
Assessments, prorating in purchase and sale transaction, 4.133
CC&Rs. See **Covenants, Conditions, and Restrictions (CC&Rs)**
Conversion of existing dwellings
Generally, 4.72
Disclosures in first sale of conversion units, 6.62

Seller's alternative, conversion into condominium, 1.31
Description of, 11.7
Disclosure requirements in residential transactions
Generally, 6.60
Davis-Stirling Act disclosures, 6.61
First sale of conversion units, disclosures in, 6.62
First sale of units in common interest development, disclosures in, 6.63
Review of disclosures by buyer, 6.74
Liquidated damages provisions in initial sale of new condominiums, special rules governing, 6.14
Property insurance for, 13.37

Common Law
Bad faith claim against property insurer under, 13.112
Brokers
Breach of fiduciary duty by broker, common law remedies for, 2.153
Honesty and fair dealing, common law obligations of, 2.178
Salespersons and brokers, relationship under common law, 2.16
Disclosure. See **Disclosure**
Fraudulent conveyances, challenging on common law grounds, 10.13
Rule against perpetuities, abolishment of common law in favor of statutory construction, 8.16

Community or Separate Property
See also **Homestead Property**
Generally, 6.89
Changing title from joint tenancy to community property, grantee recital, 10.34
Deeds. See **Deeds**
Execution, spousal signature or waiver, 4.19
Married woman acquiring property, separate property presumption, 10.29
Method of taking title, 4.21
Nature of ownership, 10.29, 10.33
Presumption, 4.21, 10.26, 10.29
Right of survivorship, community property with, 6.91

Compensation. See **Salaries and Compensation**

Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA). See **Hazardous Materials and Toxic Waste**

Computers
See also **Internet**
Definition of computer fraud, 13.66
Digitized images, recordation of, 15.88
Property insurance covering. See **Property Insurance**

Concealment
Liability insurance policy, claims for concealment without property damage not covered under, 14.22

Condemnation and Eminent Domain
Description of property, effect on, 11.87
Easement by necessity, failure to acquire by eminent domain, 11.56
Letter of intent on lease execution, effect on condemnation compensation, 3.19
Option agreement, effect of condemnation of property on. See **Options**
Purchase agreement provision regarding condemnation, 4.138
Releasing parcel from lien resulting from award, 9.110
Right of first refusal, condemnation for public need preempting, 8.29

Condominiums. See **Common Interest Developments**

Confidentiality
See also **Disclosure**
Constructive trust, imposition if title obtained through fraud, mistake, or constructive fraud through violation of fiduciary or confidential relationship, 10.19
Environmental consultant performing contamination due diligence study, 7.43
Letters of intent, 3.11, 3.18, 3.45
Purchase and sale agreement, 4.178

Conflict of Interest
Attorneys
Client's property, handling, 1.12
Disclosure of conflict to client, 1.7, 1.9
Equity interest as fee for legal service, 1.21
Representing more than one client, informed consent, 1.10-1.11

Rules of professional conduct, 1.6-1.11
Broker's duty to avoid. See **Brokers, Dealers, and Real Estate Salespersons**
Escrow holder's neutrality in conflict of interest between parties to escrow, 15.94

Consent
Attorney transaction
Acquiring adverse interest, client consent, 1.7
Determining consents needed from others, 1.10, 1.66-1.67, 1.92
Direct communications with client represented by counsel, consent required, 1.117
Fees, client's informed consent required, 1.19
Representing more than one client, informed consent, 1.10-1.11
Brokerage transactions, consent to dual agency, 2.129
Easement's location and scope, consent of parties fixing, 11.51
Escrow holder's consent, 4.180
Joint tenancy. See **Joint Tenancy**
Property insurance policy, insurer's written consent to assignment of, 13.24
Purchase and sale agreement
Corporate property conveyances, 4.28
FHA approval for development, 4.3
Marital property conveyance, 10.40
Parties consent, 4.6, 4.8, 4.180
Return of deposit, 1.131

Conservatorship. See **Guardianship and Conservatorship**

Consideration
See also **Contracts**
Generally, 4.6, 4.11, 4.30, 4.35, 4.169
Allocation of, 4.36
Deeds, 10.13
Minors, contracts with, 4.15
Mutuality, 4.30, 4.86
Options. See **Options**
Part performance, 4.13
Purchase and sale agreement, 4.6, 4.11, 4.35, 4.86, 4.143

Constitutional Law
CERCLA, constitutionality of clean up orders under, 7.15
Due process, federal tax lien preattachment hearing, 4.62
Punitive damages award against insurer, constitutionality of. See **Property Insurance**
Usury limitations for loan secured by real property and made or arranged by real estate broker, retroactive effect of constitutional amendment affecting, 2.9

Construction and Interpretation
See also **Definitions**
Accident, 14.19
All appropriate inquiries standards (EPA), 7.29
Ambiguities. See **Ambiguity**
Business establishment, 6.101
Contaminated property issues
Innocent landowner defense, 7.24
Secured creditor exemption, 7.88
Third party defense, 7.23
Dedication implied in fact and implied in law distinguished, 11.77
Description of property
Doctrines applicable to, 11.1
Doctrines of agreed boundaries and practical location, 11.79
Easement, description of, 11.44
Grantee, interpreting description in favor of, 10.42
Rule for construing, 11.14-11.15
Statutory rules of construction, 11.98
Streets and public rights-of-way, construing grant to center of highway absent other intent, 11.30
Easements
Descriptions of easements, generally, 11.44
Failure to designate as easement, 11.72
Grant of, 11.45, 11.49, 11.65, 11.70
Railroad rights-of-way, 11.71
Encumbrances, scope of covenant against, 4.111, 12.7
Exclusion to insurance policy, construction in favor of insured, 13.74
Good faith, improvement of lands made in, 11.114
Letters of intent, determining binding nature, 3.1, 3.3-3.4, 3.12, 3.14-3.25
Liability insurance. See **Liability Insurance for Real Property Transfers**

Listing agreement, strict construction against broker, 2.56
Marketable title, 4.50-4.51
Monument doctrine, 11.31
Pollutant, 13.86
Pre-printed form agreements, applicability of statutory rules of contract interpretation to, 6.4
Professional services, 14.71
Property insurance policy, broad construction of exceptions to exclusions, 13.75
Purchase and sale agreement, 4.158, 4.178
Recorder as agent of grantee or mortgagee, 15.92
Single purpose entity (SPE), 9.3
Spangler case, 9.95-9.98
Strict construction of deed if property acquired by public entity through private dedication, 10.2
Uniform Vendor and Purchaser Risk Act, 13.6

Construction Defects, Insurance Coverage for. See **Liability Insurance for Real Property Transfers**

Construction, Improvements, and Repairs
Building permit requirement and vested rights, 4.86, 4.89
Common law duty to disclose improvements or repairs, 6.31A-6.32
Contaminants used in buildings, 7.5
Describing improvements and appurtenances included in sale, 4.32, 4.169
Disbursing construction loan proceeds, 9.80
EIRS, 4.95-4.98
Existing promissory note's obligations, 4.39
Liability insurance, responsibility for code-mandated repairs, 13.107
Mechanics' liens. See **Mechanics' Liens**
Owner's notice of nonresponsibility, 4.78
Party walls, 4.65
Seller's alternative, changing nature of improvements, 1.31
Special assessments for public improvements, 4.63
Structural pest control corrective work, 4.79
Tenancy-in-common agreement, App O
Tenant's right, 4.73
Upper landowner changing natural drainage system, reasonableness and liability, 4.77

Constructive Notice. See **Notice and Notification**

Constructive Trust
Title obtained through fraud, mistake, or constructive fraud through violation of fiduciary or confidential relationship, imposition of constructive trust if, 10.19

Consultants
See also **Experts**
Engineers. See **Engineers**
Environmental. See **Hazardous Materials and Toxic Waste**
Form contracts, overly protective indemnity provisions, 1.69
Surveyors. See **Surveys and Surveyors**

Contaminated Property. See **Hazardous Materials and Toxic Waste**

Contractors
Independent contractors. See **Independent Contractors**
Liability insurance for contractors. See **Liability Insurance for Real Property Transfers**

Contracts
See also **Breach of Contract; Consideration**
Agency law versus contract law, 2.26
Ambiguity. See **Ambiguity**
Assignment of intangibles, App J
Assignment of leases, App I
Attorney fee agreement. See **Attorneys' Fees**
Bill of sale. See **Bill of Sale**
Brokerage industry. See **Brokers, Dealers, and Real Estate Salespersons**
Capacity to contract
Generally, 4.6-4.7, 4.14
Guardians or conservators, 4.17
Incompetent persons, 4.16-4.17
Minors, 4.7, 4.15
Prisoners, 4.18
CC&Rs. See **Covenants, Conditions, and Restrictions (CC&Rs)**
Competing offers, agreement not to solicit, 3.11
Consultants' form contracts, overly protective indemnity provisions in, 1.69

Covenants of title, damages for breach, 12.18
Escrow. See **Escrow**
Execution of contract. See **Execution of Documents**
Grant deed. See **Deeds**
Hazardous substances provisions. See **Hazardous Materials and Toxic Waste**
Installment land contract. See **Installment Transactions**
Insurance policies. See **Insurance**
Lawful object, 4.6, 4.10
Letters of intent. See **Letters of Intent**
Listing agreement. See **Listing Agreement**
Options. See **Options**
Oral. See **Oral Agreement**
Performance. See **Performance**
Pre-printed form agreements, applicability of statutory rules of contract interpretation to, 6.4
Purchase and sale. See **Purchase and Sale Agreement**
Representations and warranties. See **Representations and Warranties**
Risk of loss. See **Risk of Loss**
Specific performance. See **Specific Performance**
Statute of frauds. See **Statute of Frauds**
Subordination agreements. See **Subordination**
Withdrawal of documents, contract governing, 15.59

Conversion of Property. See **Common Interest Developments**

Co-Ownership
Common interest developments. See **Common Interest Developments**
Joint tenancy. See **Joint Tenancy**
Joint ventures. See **Joint Ventures**
Partnership. See **Partnerships**
Tenancy in common. See **Tenancy-in-Common**

Corporations
Authority to bind corporation, 4.28, 4.156
Certificates and certification
Approval of transaction by board of directors, corporation secretary certifying, 4.28
Nonforeign status, corporation's certification of, 15.82
Resolution authorizing corporate conveyances, certified copy of, 10.65
Commissioner of Corporations, enforcement of escrow law by, 15.4
Conveyances, 4.28, 4.156
Deeds
Acceptance of deed, 10.75
Grantor recitals in deed, 10.20
Signatures, 10.65
Directors and officers
CERCLA, director's and officer's personal liability under, 7.14
Letter of intent, effect of requiring board of directors to approve transaction, 3.22
Managing agent's acts or omissions, corporate entity's liability for punitive damages based on, 13.117B
Officers (see Directors and officers, above)
Real estate broker, corporation as licensed, 2.4
Resolutions
Certified copy of resolution authorizing corporate conveyances, 10.65
Purchase, board resolution authorizing, App D
Selling or buying corporate property
Bill of sale. See **Bill of Sale**
Board resolution authorizing purchase, App D
Signatures
Generally, 4.28, 4.156
Agent's signature binding on corporation, 4.28, 4.156
Deed, 10.65
Title (see Title, below)
Tenancy-in-common or joint tenancy ownership of property, 4.22
Title
Nominee taking title on behalf of entity not yet formed, 4.156-4.157
Requirement for conveying title to corporate property, 4.19
Unincorporated associations, 10.16
Yet to be formed entity purchasing property, 4.20

Costs
See also **Expenses and Expenditures; Fees**
Annexation, 4.91
Closing costs. See **Closing Costs**
Escrow. See **Escrow**

Fair Housing Act (FHA), recovery of costs under, 6.100
Letters of intent, 3.6, 3.11
Liability insurance. See **Liability Insurance for Real Property Transfers**
Loan subordination, 9.76
Maintaining party wall, 4.65
Property insurance, recovery of costs in action for breach of, 13.115
Refinancing costs, 4.38
Remediating contaminants. See **Hazardous Materials and Toxic Waste**
Structural pest control inspection reports or corrective work, 4.79
Survey costs, 4.78, 4.134
Title insurance, 1.139, 4.53, 4.122, 4.134
Title report, 4.56
Transaction costs, allocation between buyer and seller, 6.23

Cotenancy
Description of property, forms of ownership, 11.5
Joint tenancy. See **Joint Tenancy**
Option contract to purchase property, effect of co-tenant selling cotenancy interest on remaining cotenant's obligations under, 8.32
Partition of, 4.23
Partnership. See **Partnerships**
Tenancy in common. See **Tenancy-in-Common**

Covenants
Hotel purchase and sale agreement, seller's preclosing covenants, 5.14, 5.15
Implied covenants
Buyer's completion of purchase, implied covenant for, 2.120
Good faith. See **Good Faith and Fair Dealing**
Grant deeds, 4.111, 10.36, 12.5-12.7
Option contract for purchase of real property, covenants of optionor, 8.66
Recordation of covenants
Fair Employment and Housing Act (FEHA) procedures for modification of recorded covenants to remove discriminatory restrictions, 6.102
Residential facility for elderly, inapplicability of recorded covenants permitting only residential use of property to, 6.104

Covenants, Conditions, and Restrictions (CC&Rs)
Description of property, 11.7
Elimination of CC&Rs, recital in deed, 10.49
Purchase and sale transaction
Generally, 4.66
Enforceability, 4.66
Private transfer fee imposed by CC&R affecting transfer or sale of property, seller's disclosure of, 6.46A
Seller's construction covenants, 4.105
Seller's preclosing covenants, 4.172
Warranties and covenants to survive delivery of deed, 4.109, 4.111
Warranty of seller's knowledge, 4.115

Covenants of Title
See also **Representations and Warranties**
Generally, 12.1
Assignment of, 12.8, 12.20
Avoiding effect of title covenants, 12.22-12.23
Breach of covenants and remedies
Generally, 12.2, 12.4, 12.13-12.17
Attorney fees, recovery of, 12.15, 12.18
Damages, 12.18
Liability for breach, 12.20
Nonowner spouse, quitclaim deed to avoid liability, 10.56
Parties entitled to recover, 12.19
Damages
Breach, recovery of damages for, 12.18-12.19
Encumbrances, damages for breach of covenant against, 12.14
Quiet enjoyment, damages for breach, 12.15
Unrecorded interests, 12.3
Deeds. See **Deeds**
Encumbrances, covenant against
Gift deed, effect of, 10.13
Scope of covenant, 4.111, 12.7, 12.14
Fee interest. See **Fee Interest**
Fraud. See **Fraud and Misrepresentation**
Further assurance, covenant for, 12.10, 12.16
Heirs and devisees, effect of covenants, 12.11

Implied covenants, statutory grant deed, 12.5
Implied warranty of merchantability and covenant of title distinguished, 12.1
Merger into deed, 12.4
Quiet enjoyment, 12.9, 12.15
Quitclaim deeds. See **Deeds**
Recording Act, 12.2
Remedies for breach (see Breach of covenants and remedies, above)
Right to convey, 12.8, 12.13
Seisin and good title, 12.6, 12.13
Statute of limitations
Breach of title covenants, table, 12.21
Quiet enjoyment and warranty, 12.9
Seisin, 12.6
Title insurance, effect on, 12.3
Unrecorded interests, 12.3
Warranty deed covenants, 12.9, 12.12, 12.17

Criminal Activity
Brokers, criminal penalties against. See **Brokers, Dealers, and Real Estate Salespersons**
Disclosure of criminal activity on property, 6.31B
Installment land contract, failure to apply payments to existing encumbrance, 9.63
Property insurance coverage against criminal acts. See **Property Insurance**

Damages
See also **Punitive Damages**
As-is exculpatory provisions. See **As-Is Clause**
Brokers. See **Brokers, Dealers, and Real Estate Salespersons**
Covenants of title. See **Covenants of Title**
Description of property, damages for breach despite ambiguity, 11.15
Disclosures, damages for failure to make. See **Disclosure**
Emotional distress damages. See **Emotional Distress**
Hazardous substances. See **Hazardous Materials and Toxic Waste**
Insurer's duty to indemnify limited to money damages, 14.25A
Letters of intent. See **Letters of Intent**
Liquidated damages. See **Liquidated Damages**
Measure of damages
Agency situations, measure of damages in, 2.159
Breach of contract, 2.156, 15.22
Negligence. See **Negligence**
Option for purchase of real property, measure of damages for repudiation of, 8.33
Misapplied loan funds, 9.85
Mitigation of damages
Business interruption coverage, insured's duty to mitigate damages, 13.62
Default by buyer, seller's duty to mitigate damages, 6.14
Offsets. See **Offsets**
Property insurance, recovery of damages from insurer. See **Property Insurance**
Purchase and sale agreement. See **Purchase and Sale Agreement**
Recordation of document, recorder's liability for negligence in, 15.87
Release clause in purchase agreement, 9.102
Surface water runoff damages, strict liability, 4.77
Tenants remain after closing, 4.72, 4.103
Time of essence clause, recovery of monetary damages for violation of, 4.152

Davis-Stirling Act
Disabled person, condominium owner's modification of unit to facilitate access for, 6.105
Disclosures under, 6.61

Day Care
Restrictions on use or occupancy of real property, effect on family day care home for children, 6.104

Dealers. See **Brokers, Dealers, and Real Estate Salespersons**

Death
Agreement binding on successors, 4.161
Disclosure of occupant's death in residential property, 6.65
Joint tenant, death of. See **Joint Tenancy**
Option contract, transferability at optionee's death, 8.27

Decedent's Estate
Certificate of nonforeign status by estate, 15.82
Contaminated property liability, 7.22

Court approval for conveying property, 4.19
Covenants of title, effect on heirs and devisees, 12.11
Execution of deed, executor or administrator signature, 10.63
Federal estate tax lien, 4.62
Joint tenant's property interest, 4.22
Wills. See **Wills**

Declaration of Covenants, Conditions, and Restrictions. See **Covenants, Conditions, and Restrictions (CC&Rs)**

Declarations. See **Affidavits and Declarations**

Declaratory Relief
Generally, 11.113
Boundary disputes, 11.90

Dedication
Description of property, 11.57, 11.77
Easement by prescription of dedicated property, 11.57
Expired offers of dedication, 11.116
Implied dedication, 11.77
Strict construction of deed if property acquired by public entity through private dedication, 10.2

Deeds
Acceptance, 10.75
Acknowledgments. See **Acknowledgments**
After-acquired title
Covenant for further assurances, 12.10
Easement by prescription, 11.57
Grant deeds, 10.2
Quitclaim deeds, 10.4, 12.22
Community property
Grantee recitals (see Grantee recitals, below)
Spouse-to-spouse recital of separate property in deed, 10.39
Consideration, 10.13
Conveyance, words of, 10.23
Corporations. See **Corporations**
Covenants of title
Implied covenants in grant deed, 4.111, 10.36, 12.5-12.7
Merger into deed, 12.4
Definitions, 10.1
Delivery, 10.1, 10.75, 15.26
Description of property
Ambiguous deeds, 11.15, 11.25
Correcting or clarifying description, 10.42
Covenants in deed, contract clause for, 11.111
Incomplete, confusing, or erroneous descriptions, 11.91
Limits as source of description, 11.9
New deed after failure to close metes and bounds description, 11.90
Omitted or uncertain description, 10.35
Practical location doctrine, relationship between monuments and deed description, 11.79
Quitclaim deeds (see Quitclaim deeds, below)
Reference to deed or other recorded instrument, description by, 11.102
Supplemented description in later deeds adding ambiguity, 11.96
Uncertain description voiding conveyance, 11.14
Elements of deeds, 10.6
Evidence
Conflicting deeds, execution date as evidence to determine priority, 10.53
Consideration, evidence of, 10.13
Corporation's acceptance of deed, evidence of intent, 10.75
Delivery of deed, 10.73
Execution. See **Execution of Documents**
Exhibits and riders, 10.36, 10.38
First duly recorded conveyance, effect on subsequent purchaser or mortgagee, 12.2
Grant deeds
Generally, 10.2
Defined, 10.1-10.2
Delivery of, 10.1, 15.26
Form, 10.3, 10.7, App G
Implied covenants, 4.111, 10.36, 12.5-12.7
Presumption fee simple title passed, 10.2, 10.44
Recording requirements, 10.8
Restrained grant deed to avoid liability under title covenants, 12.23

Statutory, 10.3, 12.5
"Subject to" clause, 10.37
Grantee
Capacity requirement, 10.24, 10.26
Certainty requirement, 10.25
Estate, nature of, 10.28
Ownership, nature of, 10.29
Proportion of interest, 10.30
Status of grantee, 10.26
Grantee recitals
Changing title from joint tenancy to community property, 10.34
Community property, 10.33
Joint tenancy, 10.31
Tenancy-in-common, 10.32
Grantor recitals
Generally, 10.14, 10.22
Corporation, 10.20
Grantor's name different from record owner's names, 10.15
Joint venture, 10.21
Partnerships. See **Partnerships**
Trustee, 10.19
Unincorporated association, 10.16
Joint tenancy. See **Joint Tenancy**
Leases. See **Leases**
Life estates. See **Life Estates**
Minor, deed to, 10.24, 10.26
Mortgages and trust deeds. See **Financing**
Names
Certainty as to name of grantee, 10.25
Change of name, 10.15
Corporate name, 10.65
Grant deeds, requirements for recording, 10.8
Grantor's name different from record owner's name, 10.15
Joint ventures, 10.66
Partnership name, 10.64
Signatures conforming to name of grantor, 10.55
Partnerships. See **Partnerships**
Presumptions affecting. See **Presumptions and Inferences**
Quitclaim deeds
Generally, 10.4
Avoiding liability under title covenants, 12.22
Blanket descriptions in deeds for multiple parcels, 11.109
CC&Rs, elimination of, 10.49
Extinguishing easement by quitclaim, 11.108
Further assurance covenant, 12.10
Married person conveying property, deed from spouse, 4.19
Nonowner spouse, 10.56
Overlapping descriptions, 11.89
Seisin, covenant of, 12.6
Witness acknowledgment insufficient to prove execution of, 15.89
Recordation. See **Recordation of Documents**
Reservations and exceptions
Mineral rights, recital in deed, 10.51
Release of exception or reservation, recital in deed, 10.44
Special recitals
Generally, 10.38
CC&Rs, elimination of, 10.49
Consent to joint tenancy between one spouse and another person, 10.40
Conveyance in performance of sales agreement, 10.45
Conveyance on distribution of trust, 10.47
Conveyance on exercise of option, 10.46
Correcting or clarifying description of property, 10.42
Deed in lieu of foreclosure, 10.41
Life estate, 10.52
Release of exception or reservation, 10.44
Removal of power of termination, 10.50
Removing cloud on title, 10.43
Spouse-to-spouse recital of separate property, 10.39
Termination of recorded lease, 10.48
Spousal conveyances, 10.26, 10.56-10.57, 10.66
Strict construction of deed if property acquired by public entity through private dedication, 10.2
Third parties. See **Third Parties**

Title insurance. See **Title Insurance and Preliminary Report**
Trustees. See **Trusts and Trustees**
Validity. See **Void or Voidable Transactions**
Warranty deeds, 4.109, 10.5, 12.9

Default of Obligation
Acceleration of payment, 9.47
Foreclosure. See **Foreclosure**
Forfeiture of buyer's deposit on default, 6.13
Mitigation of damages by seller after buyer's default, 6.14
Redemption of property in default for unpaid tax lien, 4.60
Secured creditor coverage, payment of outstanding loan balance if default occurs and environmental condition exists at location, 13.51

Defects
Acknowledgments. See **Acknowledgments**
As is clause, effect of seller's failure to disclose known or hidden defects on, 2.185
Constructive notice of. See **Notice and Notification**
Description of property, defects in. See **Description of Property**
Latent defect, 13.86, 14.23
Liability insurance. See **Liability Insurance for Real Property Transfers**
Limited partnership interests, 4.25
Material defects defined, 6.77
Purchase and sale agreement. See **Purchase and Sale Agreement**
Question of fact, discoverability of defect on inspection as, 4.49
Title, defects in. See **Title**
Waiver of defective exercise of option, 8.23

Defenses
Assumption of encumbrance, defenses available to seller, 9.48
Bad faith. See **Good Faith and Fair Dealing**
Contribution claims, 7.16-7.20
Defects in title, inspection of property to support bona fide purchase defense, 11.75
Estoppel. See **Estoppel Doctrine**
Hazardous materials. See **Hazardous Materials and Toxic Waste**
Indemnity. See **Indemnity**
Misrepresentation, buyer's failure to investigate matters of public record not defense to, 6.73
Statute of frauds. See **Statute of Frauds**
Statute of limitations. See **Statutes of Limitations**

Definitions
See also **Construction and Interpretation**
Able buyer, 2.106
Accident, 14.18
Accommodation recording, 15.24
Accretion, 11.82
Actual cash value, 13.102
Additional insured, 14.37
Adverse possession, 11.77
Alluvion, 11.86
Appurtenant easements, 11.67-11.68
Arranger of credit, 9.10
Bodily injury, 13.47, 14.28
Bona fide purchaser, 7.34
Broker, 2.2
Business, 14.82
Business opportunity, 2.10
California Coordinate System, 11.22
Claim, 14.14A
Cleanup costs, 13.47, 13.49
Close of escrow, 4.175
Closing date, 4.175
Comfort opinions, 1.124
Community property, 6.89
Competence, 1.5
Computer fraud, 13.66
Concave, 11.34
Conditional use permits and variances, 4.87
Contaminated property terminology
Generally, 7.1
Bona fide prospective purchaser, 7.31
Contractual relationship (third party defense), 7.23

Federal statutes definitions of hazardous substances and toxic pollutants, 7.8
Friable and nonfriable asbestos-containing materials (ACMs), 7.5
Hazardous materials, 7.48
Indemnity, 7.66
Innocent landowner defense, 7.24
Phase I report, 7.37
Phase II report, 7.38
Release, 7.66
State statutes definitions of hazardous substances and toxic pollutants, 7.9
Contingency date, 4.48
Convex, 11.34
Conveyance, 10.1
Cooperating broker, 2.93
Covenant of quiet enjoyment and warranty, 12.9
Covenant of seisin, 12.6
Covenant of title, 12.1
Covenant of warranty of title (covenant of "non-claim"), 12.9
Covenants, conditions, and restrictions (CC&Rs), 4.66
Credit bid rule, 13.32
Damages, 14.51
Dealer property, 9.32
Deductible, 13.108
De facto subordination, 9.88
Distance, 11.34
Domestic partners, 6.90
Dominant tenement, 11.43
Dual agency, 2.35
Due diligence, 4.45
Duty of care, 1.14
Dwelling, 13.69
Easement, 11.43
Easement by implication, 11.54
Easement by implied reservation, 11.55
Easement by prescription, 11.57
Easement of necessity, 11.56
Easements in gross, 11.67-11.68
EIR project, 4.95
Electronic record, 2.47, 4.12
Emancipated minor, 4.15
Eminent domain, 11.87
Encumbrances, 12.7
Ensuing loss, 13.84
Episodic loss, 13.78
Equity purchasers, 6.107
Equity seller, 6.107
Escheat, 15.25
Escrow, 15.1
Escrow agent, 15.2
Escrow officer, 15.10
Essential terms, 3.21
Except, 11.101
Excepting, 11.73
Exceptions to title, 6.84
Execution, 10.54
Executory contract, 8.28
Executory subordination agreement, 9.73-9.74
Factual opinions, 1.124
Financial institution, 2.182
Finder, 2.5
Fixtures, 6.8
Fortuitous event, 13.81
Full credit bid, 13.31
Grant, 10.1, 12.5, 12.23
Grant deed, 10.1-10.2
Handicap, 6.100
Home inspection, 6.77
Home inspection report, 6.77
Home inspector, 6.77
Hotel purchase and sale agreement, definitions in, 5.9
Housing for older persons, 6.103
Impaired property, 14.68
Indemnity (property insurance), 13.99

Indemnity, 7.66
Independent escrow companies, 15.4
Indexing, 15.91
Industrial use zone, 6.46
Infill area, 7.33
Inflation guard, 13.106
Informed consent, 1.10
Installment land contract, 9.14-9.15
Insurable interest, 13.16
Insurance Services Office (ISO), 14.2
Insured, 14.32
Insured contract, 14.51
Internet escrow agent, 15.5
Joint tenancy, 6.87
Latent defect, 13.86, 14.23
Letters of intent, 3.1
Lineal warranties, 12.11
Listing agreement, 2.54
Loss, 13.47, 13.51
Lot division description, 11.40
Manifestation of loss, 13.80
Material defect, 6.77
Material facts, 2.127
Material loss, 13.5
Mortgage broker, 2.8B
Multiple listing service, 2.39
Named insured, 14.32
Natural monuments, 11.27
Natural persons, 6.82
Natural resource damage, 13.47
Neap tides, 11.82
Occurrence, 14.18, 14.47, 14.49D
Open insurance policy, 13.101
Opinion, 1.123
Option, 8.1, 9.53
Original issue discount (OID), 9.35
Partnership interest, 6.92
Personal injury, 14.69
Preliminary report, 6.80
Prescription, 11.77
Principal residence, 15.76
Procuring cause of sale, broker as, 2.99
Products-completed operations hazard, 14.67
Products or completed operations hazard, 14.57
Professional negligence, 2.142
Promissory estoppel, 3.26
Property damage, 13.47, 14.25, 14.26
Proration, 15.43
Purchase and sale terminology
  Arranger of credit, 9.10
  CC&Rs, 4.66
  Emancipated minor, 4.15
  Gross and net acreage, 4.58
  Unlawful object of contract, 4.10
  Warranty or representation, 4.107
Qualified permanent resident (senior citizen housing), 6.103
Quarters, 11.21
Range, 11.19
Real property, 6.7
Real property sales contract, 9.15, 9.17
Reasoned opinions, 1.124
Release, 7.66
Reliction, 11.82
Religion, 2.181
REO (real estate owned) sale, 6.110
Replacement cost value, 13.103
Reserving, 11.73
Residence in foreclosure, 6.107
Restoration costs, 13.47
Restrained grant deed, 12.23
Sale, 2.112
Salesperson, 2.13

Section, 11.20
Seller's broker, 2.93
Selling agent, 2.31
Senior citizen, 6.103
Senior citizen housing development, 6.103
Servient tenement, 11.43
Short sale, 6.106C
Significant impact on environment, 4.95
Special recording, 15.42
Subdivision terminology
Design and improvements, 4.92
Subdivision, 1.83, 4.92
Subject to clauses, 10.37
Suspension of operations, 13.59
Tangent, 11.34
Tangible property, 14.25
Tax terminology in calculating gain, 9.25
Tenancy in common, 6.88
Title insurer, 15.15
Trade or business, 4.36
Transaction broker, 2.38A
Transaction costs, 6.23
Transfer fee, 6.46A
Ultimate net loss, 14.25A
Underwritten title company, 15.15, 15.36
Urban area, 7.33
Valuable papers and records, 13.67
Valued insurance policy, 13.101
Warranty deed, 12.9
Water heater, 6.58
Your work, 14.67

Delay
Retroactive recordation of document as remedy for recorder's improper delay, 15.92

Delivery of Documents
Generally, 10.71
Appraisal report, 9.12
Constructive delivery, 10.74
Deeds, 10.1, 10.75, 15.26
Escrow. See **Escrow**
Grant deed, 10.1
Letter instructing tenants to pay rent to buyer, 4.73, App L
Notices regarding purchase and sale agreement, 4.151
Purchase and sale agreement. See **Purchase and Sale Agreement**
Rebuttable presumption, 10.73
Unconditional delivery, 10.72
Warranties and covenants to survive delivery of deed, 4.63, 4.109, 4.111

Delivery of Possession. See **Ownership and Possession**

Demolition. See **Destruction of Property**

Deposits
Checks. See **Checks**
Escrow. See **Escrow**
Forfeiture of buyer's deposit on default, 6.13
Letters of intent, 3.38
Listing agreement. See **Listing Agreement**
Purchase and sale agreement. See **Price**

Description of Property
Generally, 4.9, 4.31, 4.169
Abandoned property, 11.62, 11.80
Accuracy, attorney's confirmation of, 15.34
Acreage
Generally, 11.16
Covenant of seisin, effect of error in acreage conveyed, 12.6
Gross or net acreage, 4.58
ALTA and CLTAA policies, description of property in, 11.11-11.12
Ambiguities, 11.15-11.16, 11.96
Attorney-client relationship

Generally, 11.3-11.8
Responsibilities of attorney, 11.10-11.11
Boundaries. See **Boundaries**
California Coordinate System, 11.18, 11.22
CC&Rs, description of property in, 11.7
Certainty requirement, 11.14
Common interest development, 11.7
Construction of description. See **Construction and Interpretation**
Constructive notice. See **Notice and Notification**
Courses and distances
Bearings and degrees, 11.32
Curves, 11.34
General courses, 11.33
Measurements, 11.37
Monuments, 11.36
Symbols and written descriptions, 11.35
Dedication, 11.57, 11.77
Deeds as source of description. See **Deeds**
Defects in descriptions
Drafting to avoid defects (see Drafting to avoid defects, below)
Failure to close metes and bounds description, 11.90
Fraudulent or erroneous surveys, 11.93
Incomplete, confusing, or erroneous description, 11.91
Overlapping descriptions, 11.89
Successive descriptions, reservation or exception in, 11.92
Distances (see Courses and distances, above)
Doctrine of practical location, 11.79
Drafting to avoid defects
Generally, 11.94, 11.99
Ambiguity, avoiding, 11.96
Nonessential language, avoidance of, 11.95
Precise language, use of, 11.97
Rectangular survey map, description by reference to, 11.101
Reference to deed or other instrument, description by, 11.102
Statutory rules of construction, knowledge of, 11.98
Subdivision map, description by reference to, 11.100
Easements. See **Easements**
Eminent domain actions, 11.87
Evidence
Extrinsic evidence, 11.14-11.15, 11.98
General or common descriptions, 11.41
Parol evidence. See **Parol Evidence**
Experts, using for description of property, 11.8, 11.11
General or common description, 11.41
Historical background
Generally, 11.1
Base and meridian landmarks, 11.18
California sea boundary disputes, 11.82
Rectangular system of surveying, 11.17
Intangible personal property included in sale, description of, 4.34
Intent. See **Intent**
Letter of intent, 3.36
Lot division description, 11.40
Maps. See **Maps**
Metes and bounds
Generally, 11.26, 11.103
Adjoining lands, 11.29
Artificial monuments, 11.28
Courses and distances (see Courses and distances, above)
Failure to close, 11.90
Natural monuments, 11.27
North, designation of, 11.39
Quasi metes and bounds, 11.38
Railroad rights-of-way, 11.31
Streets and public rights-of-way. See **Streets, Roads, and Highways**
Monuments. See **Monuments**
Multiple parcels, 11.109
Natural hazard disclosure statement, 4.81, 6.49, 6.50, App N
Off-record easements. See **Easements**
Ownership and possession
Effect of buyer's failure to question parties in possession, 11.11
Form of ownership, 11.5

Personal property included in sale, description of, 4.33, 4.169, 11.97, 11.118
Purpose of description, 11.2
Quiet title action. See **Quiet Title**
Recorded instruments, reference to, 11.25, 11.102
Reference to adjoining landowners, 11.29
Reformation. See **Reformation**
Residential standard form agreement, description of property in. See **Residential Purchase and Sale Transactions**
Seller's due diligence, physical condition of property reviewed, 1.62
Statutory remedies
Declaratory relief, 11.113
Destroyed land records, remedy in rem in event of, 11.117
Expired offers of dedication, effect of, 11.116
Good faith improver, 11.114
Marketable record title, 11.115
Quiet title action, 11.112
Streets and roads. See **Streets, Roads, and Highways**
Subdivisions, 4.31, 11.4, 11.8, 11.24, 11.100
Subordination agreement, 9.76
Sufficiency of description
Acreage, 11.16
Ambiguities, 11.15
Purchase and sale agreement, 4.31
Surveys. See **Surveys and Surveyors**
Title company. See **Title Company**
Title insurance and preliminary report. See **Title Insurance and Preliminary Report**
Title. See **Title**
Void transactions. See **Void or Voidable Transactions**
Water. See **Water and Water Rights**
Zoning, 11.4

Destruction of Property
Option contract to purchase real property, effect of destruction of property on, 8.30-8.31
Party wall maintenance obligation, effect of, 4.65
Risk of loss. See **Risk of Loss**
Termination of easement on destruction of servient tenement, 11.60

Destruction of Records
Remedy in rem to establish record title in event of destroyed land records, 11.117

Detrimental Reliance
Boundary changed by estoppel, substantial improvements made, 11.88
Letters of intent, 3.3, 3.14, 3.26

Developers
See also **Subdivisions and Subdivision Map Act**
Coastal zone property, 4.88
Contaminated property liability, 7.12
Converting dwellings into common interest developments, 4.72
Development density pricing method, 4.35
Engineering studies affecting flow of surface waters, 4.77
Environmental impact reports, 4.95-4.98
FHA approval for development, 4.3
Releasing parcels from seller's lien as development progresses. See **Releases**
Seller's alternative, developing property, 1.31
Zoning issues. See **Zoning**

Directors of Corporation. See **Corporations**

Disabled Persons
Davis-Stirling Act permitting condominium owner to modify unit to facilitate access for, 6.105
Fair Housing Act (FHA), discrimination against handicapped persons prohibited under, 6.100
Guardians or conservators for people under legal disability, 4.17

Disasters
Earthquakes. See **Earthquakes and Seismic Activity**
Floods. See **Floods**
Property taxes, transferring base-year value of damaged property to comparable replacement property, 6.96

Disbursements
Construction loan disbursements, 9.80, 9.85
Escrow. See **Escrow**

Disciplinary Proceedings
Attorneys. See **Legal Ethics**
Brokers and salespersons. See **Brokers, Dealers, and Real Estate Salespersons**
Equity interest as fee for legal services, disciplinary proceedings resulting from, 1.21
Multiple parties, attorney's liability for representing, 1.11

Disclaimer
Covenants of title, disclaimer in deed, 12.23
Letters of intent, 3.16, 3.24

Disclosure
See also **Confidentiality**
"As-is" clause, effect on seller's duty to disclose, 6.9
Attorney's conflict of interest, disclosure to client, 1.7, 1.9
Brokers and salespersons. See **Brokers, Dealers, and Real Estate Salespersons**
Common interest development disclosures. See **Common Interest Developments**
Common law duty to disclose
Generally, 6.30
Easement's existence, disclosure of, 6.31A
Exempt transactions, applicability of common law duty of disclosure to, 6.35
Improvements and repairs, disclosure of, 6.31A-6.32
Material facts, disclosure of, 6.31
Scope and extent of disclosure, 6.32A
Condition of property, seller's disclosure obligations, 4.49, 4.112, 4.120, 4.173
Damages for failure to make
Common law duty of disclosure, damages as remedy for breach of, 6.30
First sale of conversion units, damages for failure to make required disclosures in, 6.62
Hazardous substances, seller's failure to disclose, 7.36
Transfer disclosures, effect of transferor's failure to make required, 6.35
Davis-Stirling Act, disclosures under, 6.61
Easements. See **Easements**
Environmental hazards
Mandatory disclosure, 6.53
Voluntary disclosure, seller providing buyer with consumer booklet on environmental hazards, 6.54
Escrow. See **Escrow**
Family members. See **Family Members**
Federal Truth in Lending Act, 9.13
Financing by seller (see Seller financing, below)
Hazards
Environmental hazards (see Environmental hazards, above)
Hazardous substances. See **Hazardous Materials and Toxic Waste**
Natural hazards (see Natural hazards, below)
Water heater compliance statement, 6.58
Health and safety disclosures
Drug lab cleanup order, notice to prospective buyer of, 6.55
Earthquakes. See **Earthquakes and Seismic Activity**
Environmental hazards (see Environmental hazards, above)
Lead-based paint disclosure, 6.51
Registered sex offenders (Megan's Law), disclosure of information about data base of, 6.56
Smoke detector compliance statement, 6.57
Structural pest control inspection report, 6.59
Loan charges, disclosure of, 2.8
Local disclosure and transfer requirements
Local Option Real Estate Transfer Disclosure Statement, 6.38
Local Transfer Disclosure Statement, 6.39
"Point of sale" ordinances, effect of, 6.41
Residential building records report, 6.40
Natural hazards
Generally, 6.47
Earthquakes. See **Earthquakes and Seismic Activity**
Flood hazards, 4.81, 6.48, App N
Natural hazard disclosure statement, 4.81, 6.49, 6.50, App N
Natural hazard zones, disclosure of, 6.48
Nontraditional and subprime mortgage products, disclosure and compliance requirements for, 2.8A
Professional liability insurance, attorney's required disclosure regarding, 1.12A
Public policy limitations on duty to disclose, 6.33
Quitclaim deed, disclosure of facts affecting value, 12.22
Representations and warranties
Generally. See **Representations and Warranties**
Hazardous substances. See **Hazardous Materials and Toxic Waste**
Purchase and sale agreement. See **Purchase and Sale Agreement**
Residential transactions

Generally, 6.29
Common law standards (see Common law duty to disclose, above)
Encroachments and easements, disclosure of, 11.76
Hazardous substances, 7.36
Nontraditional and subprime mortgage products, disclosure and compliance requirements for, 2.8A
Real Estate Settlement Procedures Act (RESPA), advance disclosure of settlement costs under, 15.95
Seller financing, 9.6
Statutory disclosure requirements (see Statutory disclosure requirements, below)
Transfer disclosures (see Transfer disclosures, below)
Safety disclosures (see Health and safety disclosures, above)
Seller financing
Generally, 6.69, 9.13
Appraisal report, 9.12
Arranger of credit, 9.10, 9.13
Balloon payment, 9.11
Seller Financing Addendum and Disclosure (CAR SFA), 9.13
Statutory disclosure requirements
Generally, 6.34
Common interest development disclosures. See **Common Interest Developments**
Death or illness of occupant of property, 6.65
FHA/HUD inspection disclosure, 6.67
Financing by seller (see Seller financing, above)
Flood disaster insurance requirements, 6.68
Health and safety disclosures (see Health and safety disclosures, above)
Home energy rating program, booklet covering, 6.70
Natural hazards (see Natural hazards, above)
New home sales, 6.64
Title insurance, notice regarding advisability of purchasing, 6.66
Transfer disclosures (see Transfer disclosures, below)
Taxes (see Transfer disclosures, below)
Transfer disclosures
Generally, 6.35, 6.38
Changed circumstances, effect on transfer disclosure, 6.35
Former federal or state ordnance locations, written notice to buyer of, 6.44
Industrial use zone, disclosures requirements if property adjacent to, 6.46
Local disclosure and transfer requirements (see Local disclosure and transfer requirements, above)
Mello-Roos Community Facilities Act or Improvement Bond Act of 1915, seller obtaining disclosure notice regarding special tax or assessment under, 6.42
Private transfer fee imposed by CC&R affecting transfer or sale of property, seller's disclosure of, 6.46A
Property taxes, exemption for transfers resulting from failure to pay, 6.35
Real Estate Transfer Disclosure Statement, 6.36, 6.37
Supplemental property tax bill, notifying prospective buyer of, 6.43
Window security bars and safety release mechanisms, seller's disclosure of existence of, 1.59, 6.45
Unrecorded interests in property, seller's duty to disclose, 6.81

Discovery
Broker, limits on discovery in disciplinary proceedings against, 2.173
CERCLA, discovery rule for personal injury or property damage under, 7.20
Question of fact, discoverability of defect on inspection as, 4.49

Discrimination in Housing Market
Generally, 6.98
Broker's liability to third parties for, 2.181
CC&Rs, racial restrictions in, 4.66
Federal laws
Civil Rights Act of 1866, remedies under, 6.99
Fair Housing Act. See **Fair Housing Act (FHA)**
Local ordinances prohibiting housing discrimination, 6.106
Senior citizen housing, exemption for, 6.103
State laws
Fair Employment and Housing Act (FEHA), 6.102
Family day care home for children, effect of restrictions on use or occupancy of real property on, 6.104
Unruh Civil Rights Act. See **Unruh Civil Rights Act**

Dismissal of Action
Escrow holder's motion to dismiss escrow holder from action after filing interpleader, 15.98

Disposal of Contaminants. See **Hazardous Materials and Toxic Waste**

Dissolution of Marriage
Disclosure requirements, exemption for transfers between spouses in connection with marital dissolution proceedings, 6.35

Documentary Transfer Tax
Exemption for changing title from joint to community property, 10.34
Separate statement of documentary transfer tax, 10.11, 10.12

Domestic Partners
Title held by registered domestic partners, 6.90-6.91

Downpayments
Cash downpayment, 9.40

Drugs
Disclosure of drug lab cleanup order to prospective buyer, 6.55

Dual Agency of Listing Agents. See **Brokers, Dealers, and Real Estate Salespersons**

Due Diligence
See also **Investigations**
Broker's lack of due diligence as grounds for revoking listing, 2.83, 2.148
Buyer's due diligence
Generally, 6.71
Checklists (see Checklists, below)
Conditional sales agreement providing time for buyer to conduct due diligence, 4.46, 4.48
Home inspection, 6.77
Investigation, buyer's duty of, 6.73
Scope of, 6.74
Self-protection, buyer's duty of, 6.72
Checklists
Buyer's comprehensive commercial property acquisition, App C
Materials seller delivers to buyer in sales involving commercial leases, App B
Condition of title to property
Preliminary report and exceptions, 4.171
Review of, 1.61
Contaminated property. See **Hazardous Materials and Toxic Waste**
Defined, 4.45
Hotel purchase and sale agreement. See **Hotels and Motels**
Legal feasibility of intended use
Applicable laws, effect of, generally, 1.73
Federal laws, 1.87-1.90
Local and regional laws, 1.74-1.80
Necessary approvals, 1.72
State laws, 1.81-1.86
Legal opinions, additional due diligence to prepare, 1.125
Length of due diligence period, 4.48
Letters of intent, 3.11
Purchaser's precontract due-diligence matters
Generally, 1.58, 4.45
Conditional sales agreement providing time for buyer to conduct due diligence, 4.46, 4.48
Condition of title to property (see Condition of title to property, above)
Consents from others, 1.10, 1.66-1.67, 1.92
Economic feasibility of intended use, 1.91
Financing purchase, review of, 1.71
Legal feasibility of intended use (see Legal feasibility of intended use, above)
Methods of providing for due diligence, 4.46
Objectives of, 1.70
Purpose of due diligence conditions, 4.47
Satisfying performance conditions of agreement, 4.47
Seller's precontract due-diligence matters
Generally, 1.58, 4.49
Conditional sales agreement requiring seller to make documents regarding property accessible for buyer's inspection, 4.48
Condition of property, review of, 1.62-1.64
Condition of title, review of, 1.61
Consents from others, 1.66-1.67
Experts, determining need for, 1.69
Financing, obtaining, 4.3
Legal issues affecting property, review of, 1.65
Natural hazard disclosure statement, 4.81, 6.49, 6.50, App N
Objectives, 1.59
Purchaser's perspective, review of from, 1.68
Valuation considerations, 1.60
Subdivision Map Act, purchaser due diligence considerations under, 1.79
Title review by attorney, 4.19

Due-on-Sale/Encumbrance Clauses
See also **Financing**
Generally, 9.48
Enforceability, 9.50-9.51
Impact on buyer, 4.43, 9.49, 9.53
Option not violation of due-on-sale provision, 9.53
Prepayment penalties prohibition, 9.52

Due Process
Federal tax lien, preattachment hearing, 4.62

Duty to Defend. See **Liability Insurance for Real Property Transfers**

Earnings. See **Salaries and Compensation**

Earthquakes and Seismic Activity
See also **Landslides and Subsidence**
Disclosure and due diligence
Generally, 1.59, 1.86, 6.48, 6.52
Natural hazard disclosure statement, 4.81, App N
Insurance coverage against
Generally, 13.52
Exclusions, 13.87
Revival of insurance claims resulting from 1994 Northridge earthquake, 13.93

Easements
Generally, 11.44
Access to property
Fee owner posting notice of permission excluding easement by prescription, 11.77
Necessity, easement of, 11.56
Acreage, effect of easements and rights-of-way, 11.16
Adjoining landowner-purchaser's considerations, 4.130
Adverse possession
Prescription, easement by, 11.77
Termination of easement by adverse possession, 11.64
Appurtenant or in gross
Generally, 11.67-11.69, 11.80, 11.97
Transfer of appurtenant easement, 4.32, 11.106
Change in use, 11.6, 11.66
Construction and interpretation. See **Construction and Interpretation**
Covenant against encumbrances, 4.111, 12.7
Creation of easement, 11.107
Description of
Generally, 11.6
Ambiguous description, 11.70
Amendment of written descriptions by actual location, 11.48
Disclosure of easement
Common law duty to disclose existence of, 6.31A
Encroachments and easements, disclosure of, 11.76
Underground pipeline easement, duty to disclose, 11.11
Doctrine of practical location, 11.48
Dominant and servient tenement, 11.43, 11.65-11.66
Duration of, 11.71
Exception, creating easement by, 11.73
Exclusive and nonexclusive easements distinguished, 11.74
Exclusivity of easements, 11.52
Exercise of general grant of easement in particular course or manner, 11.51
Extrinsic evidence, interpretation of grant by, 11.49
Failure to designate as easement, 11.72
Fee interest. See **Fee Interest**
Future needs, accommodation of, 11.50
Implied dedication, 11.77
Intent
Abandon easement, establishing intention, 11.62
Appurtenant or in gross easements, distinguishing by parties' intent, 11.67
Implication, easements by, 11.54
Merger, intent to prevent termination by, 11.59
Reservation in stranger, defeating grantor's intent, 11.65
Limitation to use of specified width, 11.45
Marketability of title, effect on, 4.64-4.65
Notice

Generally, 4.64
Fee owner posting notice of permission precluding easement by prescription, 11.57, 11.77
Off-record easements
Generally, 11.53
Implication, easements by, 11.54
Implied reservation, easement by, 11.55
Necessity, easement by, 11.56
Prescription, easement by, 11.57, 11.77
Ownership of
Necessity, easement by, common ownership requirement, 11.56
Prescription, easement by, 11.57
Record of ownership, consistency with, 11.6
Termination by merger, 11.59
Termination by owner's acts, 11.61
Party wall use, 4.65
Perpetual easements, 11.80
Purchase and sale agreement. See **Purchase and Sale Agreement**
Purposes and limitations, failure to state, 11.74
Railroad rights-of-way, 11.31, 11.71
Release of, 11.108
Remediation purposes, 7.85, 7.94
Reservation of easement in grantor, 11.73, 11.105
Restrictions considered negative easements or equitable servitudes, 4.66
Subdivision map, right to use streets and alleys reflected on, 11.46
Termination
Generally, 11.58
Abandonment, 11.62
Adverse possession, 11.64
Destruction of servient tenement, 11.60
Incompatible use or misuse, 11.61
Merger, termination by, 11.59
Nonuse of easements acquired by prescription, 11.63
Uncertain duration of easement, 11.71
Title review by buyer, review of easements as part of, 6.80
Transfer of property, effect on easements, 10.2
Utilities, 4.64, 11.47, 11.57, 11.62
Visible easements, 4.64
Water
Irrigation ditches, easement by implied reservation, 11.55
Standpipes for water pipeline, easement for, 4.64

Elderly Persons. See **Senior Citizens**

Elections
Tax reporting, electing not to apply installment method, 9.24

Electronic Signature. See **Execution of Documents**

Embezzlement. See **Misappropriated Funds**

Eminent Domain. See **Condemnation and Eminent Domain**

Emotional Distress
Liability insurance policy, effect of physical injury on recovery of damages for emotional distress, 14.29-14.30
Property insurance policy, recovery of emotional distress damages for breach of, 13.114

Employers and Employees
Hotel purchase and sale agreement provisions covering employees, 5.18, 5.19
Notice requirements for employee layoff, 5.18
Property insurance policy, exclusion of losses due to employee dishonesty, 13.41-13.43
Salesperson as employee of real estate broker, 2.15

Encroachments
Land survey, 4.65, 4.67
Purchase and sale agreement, 4.58-4.59, 4.67

Encumbrances. See **Liens and Encumbrances**

Endangered Species
California Endangered Species Acts, 7.1

Endorsements. See **Insurance**

Energy
Home energy rating program, disclosures concerning, 6.70

Engineers
See also **Surveys and Surveyors**
Description of property, 11.12
Environmental consultants. See **Hazardous Materials and Toxic Waste**
Liability insurance for, 14.6
Studies and reports, 4.77-4.78

Environmental Impact Report (EIR), 4.95-4.98

Environmental Protection
Disclosure of environmental hazards. See **Disclosure**
Hazardous materials. See **Hazardous Materials and Toxic Waste**

Equipment
Hotel equipment, 5.10

Equitable Relief
Easements, preventing merger and termination of, 11.59
Estoppel. See **Estoppel Doctrine**

Equity Interests
Fee for legal services, equity interest as, 1.21
Purchaser's alternative, equity sources as, 1.35
Seller's alternative, equity sources as, 1.30

Escrow
See also **Financing**
Acknowledgments
Escrow instructions, escrow holder's acknowledgment of. See **Escrow Instructions**
Execution of documents. See **Execution of Documents**
Allocation of funds and expenses
Closing costs. See **Closing Costs**
Prorations (see Proration of expenses, below)
Arranger of credit exception, escrow agent, 9.10
Assignments
Irrevocable assignment language, effect on broker's commission, 15.94
Proceeds, broker's enforceability against escrow holder of party's assignment of, 15.14
Proceeds, effect of seller assignment of, 15.30
Attorney fees and costs
Escrow holder's recovery of, 15.98
Escrow instructions, allocation of fees in, 15.31, 15.58
Purchase agreement's allocation of fees in, 15.42
Attorneys
Buyer's and seller's attorneys not parties to escrow, 15.12
Description of property, attorney's confirmation of accuracy of, 15.34
Drafting escrow instructions. See **Escrow Instructions**
Duty owed escrow agent, 9.4-9.5
Escrow holder (see Escrow holder, below)
Exemption of attorneys from escrow law, 15.6
Fees (see Attorney fees and costs, above)
Bank's exemption from escrow law, 15.6
Breach of covenant (see Closing escrow, below)
Brokers
Assignments (see Assignments, above)
Commission (see Broker's commission, below)
Decision to use broker as escrow agent, 2.23
Deposits by buyer, handling of, 4.37
Escrow holder, real estate broker acting as, 15.2
Exemption of real estate brokers from escrow law, 15.6
License requirements for broker acting as escrow agent, 2.22
Parties to escrow, brokers for buyer and seller not, 15.14
Post-closing fiduciary duties of, 2.126
Broker's commission
Generally, 15.94
Demand to escrow for payment of commission, broker submitting, 15.14
Irrevocable assignment language, effect of, 15.94
Listing agreement specifying broker's commission paid only on close of escrow, 2.110
Seller's supplemental escrow instructions for payment of, 15.70

California withholding requirements
Buyer's obligation for withholding requirement, 15.79
Computation of estimated gain or loss (FTB Form 593-L), App T
Foreign Investment in Real Property Tax Act (FIRPTA) withholding requirements distinguished, 15.84
Individual exemptions to withholding requirements, 15.76
Individuals, lack of waiver for, 15.78
Installment sales (see Installment sales, below)
Non-individual exemptions to withholding requirements and waiver, 15.77
Penalties for failure to withhold, 15.79
Real estate withholding certificate for (FTB Form 593-C), App U
Statutory basis for, 15.75
Certificates
Foreign Investment in Real Property Tax Act (FIRPTA) certification, App W
Withholding requirements (see Withholding requirements, below)
Closing costs. See **Closing Costs**
Closing escrow
Breach of covenant of seisin, cause of action survives closing, 12.6
Breach of covenant of title, cause of action surviving close, 12.4
Building permits, obtaining before closing, 4.86-4.89
Clearing mechanics' liens, 4.69, 4.172
Closing process, explaining to client, 1.131
Date, setting or extending, 4.79, 4.86
Defining close of escrow, 4.175
Escrow instructions. See **Escrow Instructions**
Federal tax liens, 4.62
Funds, disbursement of, 15.93
Insurance coverage, 4.106, 4.139, 4.172
Listing agreement specifying broker's commission paid only on close of escrow, 2.110
Possession of property at close of escrow, 2.73
Postclosing follow-up, 1.140-1.144
Procedure for closing, 15.55
Processing and dispersing documents, escrow holder's responsibilities for, 15.93
Purchase and sale agreement (see Purchase and sale agreement provisions, below)
Real Estate Settlement Procedures Act. See **Real Estate Settlement Procedures Act (RESPA)**
Recordation. See **Recordation of Documents**
Structural pest control inspection before closing, 4.79
Tenants in possession, 4.72, 4.103, 4.136
Zoning confirmed before closing escrow, 4.86
Commission (see Broker's commission, above)
Commissioner of Corporations, enforcement of escrow law by, 15.4
Conditions of deposit
After conditions satisfied, title to deposits in escrow passing to other parties, 15.28
Before conditions satisfied, title to property remaining with party depositing property, 15.27
Waiver of conditions, 15.29
Costs
Closing costs. See **Closing Costs**
Court costs (see Attorney fees and costs, above)
Remediation costs, payment security, 7.60, 7.79, 7.80
Creation of escrow, 15.7, 15.13
Definitions
Accommodation recording, 15.24
Escheat, 15.25
Escrow, 15.1
Escrow agent, 15.2
Escrow officer, 15.10
Independent escrow companies, 15.4
Indexing, 15.91
Internet escrow agent, 15.5
Principal residence, 15.76
Proration, 15.43
Special recording, 15.42
Title insurer, 15.15
Underwritten title company, 15.15, 15.36
Delivery
Funds, effect of delivering to escrow, 15.26
Outside escrow, delivery of documents, 4.175
Premature delivery of title by escrow holder, effect of, 15.27
Supplemental escrow instructions concerning delivery of documents, 15.41
Deposits
Generally, 4.37, 4.170, 4.175
Broker's authority and handling of buyer's deposits, 4.37
Buyer's supplemental instructions about deposits, 15.51

Cancellation of escrow, right to obtain deposit on, 15.26
Cash downpayment, 9.40
Common account, general provisions of form instructions disclosing practice of depositing funds in, 15.36
Conditions of deposit (see Conditions of deposit, above)
Creation of escrow by depositing loan funds in connection with escrow instructions, 15.7, 15.13
Delivery of funds to escrow, effect of, 15.26
Disbursements (see Disbursements, below)
Interest on, 4.37, 4.170, 15.37
Letter of intent, deposits into escrow, 3.38
Listing agreement provisions. See **Listing Agreement**
Mechanics' lien fund, 4.69
Misappropriated funds, 15.22, 15.27
Return of (see Return of deposit, below)
Supplemental escrow instructions. See **Escrow Instructions**
Wire transfers, 4.35
Disbursements
Buyer's supplemental escrow instructions about authorized disbursements, 15.58
Cashier's, certified or teller's checks, disbursement of, 4.35
Close of escrow, disbursement of funds on, 15.93
Closing costs. See **Closing Costs**
Escrow instructions. See **Escrow Instructions**
Holdbacks, 15.96
Release of funds after breach, 4.37
Release of funds on cancellation of sale transaction, 4.100
Return of deposit (see Return of deposit, below)
Seller's supplemental escrow instructions about authorized disbursements, 15.69
Time limitations, 4.35
Disclosures
Escrow holder, disclosures by (see Disclosures by escrow holder, below)
General provisions of form instructions disclosing practice of depositing funds in common account, 15.36
Disclosures by escrow holder
Fraud, escrow holder's duty to disclose, 15.21
Material matters, escrow holder's disclosure to parties of, 15.20
Duties of escrow holder
Ambiguous, conflicting, or erroneous escrow instructions, escrow holder's duty to seek clarification of, 15.18
Disclosure to parties (see Disclosures by escrow holder, above)
Fiduciary responsibilities of escrow holder, 15.19
Fraud, escrow holder's duty to disclose, 15.21
Limited agency relationship between escrow holder and parties to escrow, 15.18
Escrow holder
Acknowledging signatures on escrow documents, 15.93
Assignment of proceeds by party to escrow, enforceability by broker against escrow holder, 15.14
Attorney as, 15.2, 15.26
Attorney fees and costs, recovery of, 15.98
Attorneys and real estate brokers acting as, 15.2
Attorney's lack of duty to, 15.12
Broker acting as, 15.2
Closing escrow (see Closing escrow, above)
Commingling of funds by, 15.36
Conflict of interest between parties, escrow holder's neutrality, 15.94
Consent of, 4.180
Defined, 15.1
Deposits (see Deposits, above)
Disclosures by escrow holder (see Disclosures by escrow holder, above)
Duties of escrow holder (see Duties of escrow holder, above)
Fraud (see Fraud, below)
Functions of escrow holder, 15.16-15.17
Good faith. See **Good Faith and Fair Dealing**
Instructions. See **Escrow Instructions**
Interpleader, escrow holder filing, 15.97-15.98
Liabilities of escrow holder (see Liabilities of escrow holder, below)
Listing agreement designating, 2.71, 2.72
Misappropriation of funds, 15.22, 15.27
Negligence. See **Negligence**
Persons eligible to be escrow holder, 15.2
Premature delivery of title by escrow holder, effect of, 15.27
Slander of title by, 15.22
Tortious conduct, escrow holder's liability for, 15.22
Execution of documents. See **Execution of Documents**
Exemptions
Generally, 15.6
Withholding requirements (see Withholding requirements, below)

Expenses
Allocation of (see Allocation of funds and expenses, above)
Proration of (see Proration of expenses, below)
Failed transactions
Cancellation of escrow, 15.97
Interpleader, escrow holder filing, 15.97-15.98
Foreign Investment in Real Property Act (FIRPTA), withholding requirements under. See **Foreign Investment in Real Property Tax Act (FIRPTA)**
Fraud
Disclosure of fraud by escrow holder, 15.21
Punitive damages, recovery against escrow holder for fraud, 15.23
Funds
Closing costs. See **Closing Costs**
Deposits (see Deposits, above)
Disbursements (see Disbursements, above)
Proration (see Proration of expenses, below)
Hotel purchase and sale agreement. See **Hotels and Motels**
Impound accounts
Loan payments, 4.133
Seller's separate escrow instructions, impound account transferred to buyer, 4.133
Subdivision offerings payments under real property sales contract, 9.17
Independent escrow companies
Generally, 15.4
Claim against, 15.4
Regulation of, 15.4
Title insurance companies distinguished from independent escrow companies, 15.15
Installment sales, withholding requirements for
Generally, 15.79
Real estate withholding installment sale agreement (FTB Form 593-I), App V
Insurance. See **Insurance**
Letter of intent, 3.43
Liabilities of escrow holder
Accommodation recording by escrow holder without assumption of liability, 15.24
Escheated funds, escrow holder's lack of liability for turning over to State, 15.25
Exculpatory clauses, 15.31
Non-parties, liability to, 15.23
Parties to escrow, liability to, 15.22
Wrong party, escrow holder's liability for paying, 15.30
License
Broker acting as escrow agent, license requirements for, 2.22
Revocation or suspension of escrow company's license by Commissioner of Corporations, 15.4
Mechanics' liens, 4.69, 4.172
Notice. See **Notice and Notification**
Opening of escrow (see Procedures for escrow, below)
Parties to escrow
Generally, 15.9
Attorneys for buyer and seller not parties to escrow, 15.12
Brokers for buyer and seller not parties to escrow, 15.14
Buyers and sellers, 15.11
Escrow holder (see Escrow holder, above)
Escrow law, parties exempt from, 15.6
Escrow officers, 15.10
Lenders, 15.13
Termination of escrow by parties (see Termination of escrow, below)
Title insurer, 15.15
Penalties. See **Penalties**
Procedures for escrow
Closing escrow (see Closing escrow, above)
Instructions. See **Escrow Instructions**
Title company or private escrow company, opening escrow at, 6.2
Proration of expenses
Generally, 4.133, 4.175
Buyer's supplemental escrow instructions, 15.57
Insurance premiums, 15.45
Interest on existing loan, 4.133
Personal property taxes, 4.61
Real property taxes, 4.60, 15.44
Rents, 4.72, 4.133, 4.175
Supplemental escrow instructions, 15.43-15.46, 15.68
Purchase and sale agreement provisions
Attorney fees, allocation of, 15.42
Closing through escrow, 4.132

Closing with tenants in possession, 4.72, 4.103, 4.136
Deposits (see Deposits, above)
Prorating expenses (see Proration of expenses, above)
Structural pest control inspection before closing, 4.79
Recordation. See **Recordation of Documents**
Regulation of escrow companies
Generally, 15.3
Independent escrow companies, 15.4
Internet escrow agents, 15.5
Northern California versus Southern California, distinctions in handling escrows, 15.8
Parties exempt from escrow law, 15.6
Release of funds (see Disbursements, above)
Rents. See **Rents**
Reports. See **Records and Reports**
Return of deposit
Generally, 4.37, 4.47, 4.100, 4.170
Consent of parties required, 1.131
Specific performance. See **Specific Performance**
Taxes
California withholding requirements (see California withholding requirements, above)
Federal tax liens, 4.62
Proration of taxes (see Proration of expenses, above)
RESPA. See **Real Estate Settlement Procedures Act (RESPA)**
Termination of escrow
Cancellation of escrow, 15.26, 15.97
Close of escrow (see Closing escrow, above)
Third party demands, impact on closing of transaction, 15.30
Time. See **Time**
Waiver
Conditions of deposit, waiver of, 15.29
Withholding requirements (see California withholding requirements, above)
Withholding requirements
California withholding (see California withholding requirements, above)
FIRPTA. See **Foreign Investment in Real Property Tax Act (FIRPTA)**

Escrow Instructions
Acknowledgments
Buyer's supplemental escrow instructions, escrow holder's acknowledgment of, 15.61
Seller's supplemental escrow instructions, escrow holder's acknowledgment of, 15.73
Additional instructions (see Supplemental escrow instructions, below)
Ambiguous escrow instructions
Escrow holder's duty to seek clarification of ambiguous, conflicting, or erroneous instructions, 15.18
Supplemental instructions to clarify ambiguities (see Supplemental escrow instructions, below)
Amended instructions, effect of, 15.18, 15.30
Buyer and seller instructing escrow holder, 15.11
Buyer's escrow instructions
Concluding provisions, 4.132
Supplemental instructions (see Buyer's supplemental escrow instructions, below)
Time for close of escrow, 4.132
Buyer's supplemental escrow instructions
Generally, 15.49
Acknowledgment of instructions by escrow holder, 15.61
Approval of documents by buyer, 15.60
Attorney fees, allocation of, 15.58
Authorized disbursements, costs, 15.58
Conditions precedent to close of escrow, 15.52
Deposits by buyer, 15.51
Estimated closing statement, 15.54
Introduction, 15.50
Procedure for closing, 15.55
Proration of expenses, 15.57
Time for closing escrow, investment of funds, 15.56
Title insurance requirements, 15.53
Withdrawal of documents or funds, 15.59
California Association of REALTORS (CAR)
Adoption of Residential Purchase Agreement and Joint Escrow Instructions (CAR Contract), 15.32
California Residential purchase agreement and joint escrow introductions (CAR Form RPA-CA), 6.24
Irrevocable assignment of broker's commission, CAR contract provision for, 15.94
Cancellation instructions, 4.100, 15.97, App AA
Close of escrow
Buyer's supplemental instructions (see Buyer's supplemental escrow instructions, above)
Seller's supplemental instructions (see Seller's supplemental escrow instructions, below)

Conflicting instruction between party to escrow and third party, 15.30
Deposits (see Supplemental escrow instructions, below)
Disbursements
Buyer's supplemental escrow instructions, 15.58
Seller's supplemental escrow instructions, 15.69
General provisions
Generally, 15.31
Attorney fees, allocation of, 15.31, 15.58
Cancellation of escrow, resolving dispute over, 15.97
Common escrow account, general provisions disclosing practice of depositing funds in, 15.36
Conflict between general provisions and CAR contract, 15.32
Escrow holder sending copy of general provisions to parties, 15.32
Sample general provisions, App S
Joint escrow instructions, 15.32
Lender's instructions, 15.74
Modification or revocation of, 15.18, 15.30
Need for, 1.132
Non-party, restrictions on escrow taking instructions from, 15.30
Ordering preliminary report, 4.54
Seller's escrow instructions
Concluding provisions, 4.132
Impound account, seller's separate escrow instruction for transferring to buyer, 4.133
Supplemental instructions (see Seller's supplemental escrow instructions, below)
Time for close of escrow, 4.132
Seller's supplemental escrow instructions
Generally, 15.62
Acknowledgment of instructions by escrow holder, 15.73
Approval of documents, 15.72
Authorized disbursements, costs, 15.69
Broker's commission, payment of, 15.70
Conditions precedent to close of escrow, 15.65
Deposits by seller, 15.64
Introduction, 15.63
Procedure for closing escrow, 15.66
Proration of expenses, 15.68
Time for close of escrow, 15.67
Withdrawal of documents or funds, 15.71
Supplemental escrow instructions
Generally, 15.48
Buyer's supplemental escrow instructions (see Buyer's supplemental escrow instructions, above)
Closing and closing costs, 15.42
Commingling of funds, escrow holder's rights concerning, 15.36
Deposit of funds, 15.35-15.37
Description of property, attorney's confirmation of accuracy, 15.34
Drafting documents, 15.38
Executing and delivering documents, 15.41
Funds held, App Z
Good funds laws, effect of, 15.35
Interest on deposits, supplemental instruction about, 15.37
Lease, transfer from seller to buyer, 15.39
Priority for recording documents, 15.47
Proration of expenses, 15.43-15.46, 15.68
Seller's supplemental instructions (see Seller's supplemental escrow instructions, above)
Title insurance, negotiating form and contents with title company or title department, 15.40
Unaddressed issues or ambiguities, preparation of supplemental instructions to cover, 15.33
Written versus oral instructions, 15.7, 15.18

Estoppel Certificate
Generally, 4.73, 4.101, 4.172, App K
Covenant against encumbrances, 12.7
Deed in lieu of foreclosure, 10.41
Hotel operator, estoppel certificate from, App R
Purchase agreement dealing with buyer's approval of tenant estoppel certificates, 15.39
Tenant's estoppel certificate, 4.73, 4.101, 12.7, 15.39, App K

Estoppel Doctrine
Boundary line changed by estoppel, 11.88
Brokers
Commission, broker's inability to collect based on estoppel theory in absence of written contract, 2.51
Ostensible agency, creation of, 2.30
Insurer's failure to inform insured of time limits applicable to claim, effect of, 13.93
Letters of intent, 3.10, 3.14, 3.26

Statute of frauds, estopped from pleading, 4.13
Toxic contamination, leased property, 7.55

Ethics
Attorneys. See **Legal Ethics**
Brokers, dealers, and salespersons. See **Brokers, Dealers, and Real Estate Salespersons**

Eviction
Quiet enjoyment, breach of covenant on eviction, 12.9, 12.15
Warranty, breach of covenant on eviction, 12.17

Evidence
See also **Burden of Proof**
Agreed boundaries, 11.78
Ambiguities, extrinsic evidence interpreting, 4.159, 11.15
Certificate of acknowledgment, 10.69
Community property presumption, evidence overcoming, 4.21
Contaminated property. See **Hazardous Materials and Toxic Waste**
Deeds. See **Deeds**
Description of property. See **Description of Property**
Easement, interpretation of grant by extrinsic evidence, 11.49
Insurance. See **Insurance**
Letters of intent. See **Letters of Intent**
Parol evidence. See **Parol Evidence**
Presumptions and inferences. See **Presumptions and Inferences**
Project having substantial impact on environment, 4.95
Tax computation on installment sales, 9.25
Title search, 7.86
Unacknowledged documents, proof of, 10.70
Wraparound financing, 9.29

Exchange of Property
See also **Change of Ownership; Residential Purchase and Sale Transactions**
Like-kind exchanges
Options facilitating like-kind exchanges, 8.52
Tax-deferred exchange, desirability of, 1.101, 4.127, 4.165
Listing agreement giving broker right to commission on lease or exchange of property, 2.98
Reappraisal triggering events, App A
Tax-deferred exchange, structuring transaction as, 1.101, 4.127, 4.165, 4.178

Exclusions. See **Insurance**

Exclusive Right to Sell. See **Listing Agreement**

Execution of Documents
Acknowledgments
Escrow holder acknowledging signatures on escrow documents, 15.93
Recordation of document, acknowledgment of signature as requirement for, 15.89
Assignment of agreement, 4.155-4.157
Attorney-in-fact, 4.19, 10.60
Broker's contract, execution of, 2.47
Community property transaction, 4.19
Corporations. See **Corporations**
Counterparts, 4.160, 4.178
Deeds
Attorney-in-fact signature, 10.60
Corporate officer, 10.65
Date of, 10.53
Defined, 10.54
Executor or administrator signature, 10.63
Grantor imposing restrictions, execution of deed by, 10.50
Guardian or conservator signature, 10.22, 10.24, 10.62
Homestead declaration, 10.57
Joint tenancy, termination of, 10.58
Joint venturer signature, 10.66
Mark of executing party, 10.59
Partner signature, 10.64
Signatures, 10.55-10.56
Spouses, 10.56
Trustee signature, 10.61
Electronic signature
Digital signature distinguished, 2.47

Uniform Electronic Transactions Act, electronic signature satisfying legal requirement of signature, 4.12
Letters of intent, effect on binding nature of, 3.19, 3.24, 3.46
Limited partnership statement, 4.19, 4.25
Listing agreement, execution of, 2.86
Mortgages and trust deeds, 4.6
Option contract, signature clause, 8.80
Purchase and sale agreement
Generally, 4.12, 4.179
Buyer's agent or nominee, 4.155-4.157
Corporations. See **Corporations**
Counterparts, 4.160, 4.178
Limited liability company, 4.27
Marital property, 4.19
Risk of loss after execution, 4.137, 4.176
Subordination agreement addendum, 9.82
Supplemental escrow instructions concerning, 15.41
Witness acknowledgment insufficient to prove execution of document, 15.89

Executors and Administrators
Deeds, signatures on, 10.63

Exhibits
Deeds, exhibits and riders, 10.36, 10.38
Purchase and sale agreement, table of exhibits, 4.181

Expectations. See **Intent**

Expenses and Expenditures
See also **Costs; Fees**
Business interruption insurance coverage, recovery of expenses under, 13.55
Covenant of title, recovery of expenses on breach of, 12.19
Escrow. See **Escrow**
Hotel purchase and sale agreement, provision for proration of expenses, 5.26
Letter of intent, reliance expenditures, 3.26
Liability insurance, insurer's duty to provide investigative expenses as part of duty to defend, 14.14
Reimbursement. See **Reimbursement**

Experts
See also **Consultants**
California Land Use & Revitalization Act, recovery of expert fees under, 7.32
Compensation of, 1.57
Description of property, use of experts for, 11.8, 11.11
Engineers. See **Engineers**
Environmental consultants. See **Hazardous Materials and Toxic Waste**
Purchaser's due diligence, using experts for, 1.93
Scope of attorney's work with experts, 1.17, 1.93
Seller's due diligence, using experts for, 1.69
Surveyors. See **Surveys and Surveyors**
Tax issues, expert's assistance on, 1.20
Use of, 1.57
Work product of expert, protection of, 1.57

Expiration or Termination. See **Termination of Transaction**

Extension of Time
Contractual provisions, inapplicability of statute extending time for performance of act for acts governed by, 4.152
Liability insurance, extending reporting period for claims made policy, 14.15
Options, extension of. See **Option**

Fair Employment and Housing Act (FEHA), 6.102

Fair Housing Act (FHA)
Generally, 6.100
Broker's liability to third parties for housing discrimination under, 2.181
Development, FHA approval for, 4.3
Inspection disclosure, 6.67

Family Members
Broker's relative, disclosure of purchase by, 2.133
Transfers between persons in lineal lines of consanguinity, disclosure exemption for, 6.35

Farmland. See **Agricultural Property**

Faulty Workmanship Exclusion. See **Liability Insurance for Real Property Transfers**

Fax
Method of giving notice, 4.151

Federal Preemption
See also **Preemption**
Fair Housing Act (FHA), preemption of state and local laws under, 6.100
Federal Arbitration Act, preemption of state law by, 6.15, 6.18-6.18A

Fee Interest
Abandonment. See **Abandoned Property**
Cancellation of escrow fee, 15.97
Covenants of title
After acquired title, 12.10
Encumbrances, covenant against, 12.7
Implied covenants in statutory grant deed, 12.5
Description of property, forms of ownership, 11.5
Easements
Failure to designate as easement, fee ownership, 11.72
Prescriptive easement, 11.57, 11.77
Railroad rights-of-way grant, determining if fee or easement, 11.71
Presumptions
Grant deeds, presumption fee simple title passed, 10.2, 10.44
Nature of estate not stated on deed, presumption of fee estate, 10.28

Fees
See also **Costs; Expenses and Expenditures**
Air quality management, emissions fees, 7.7
Attorney fees. See **Attorneys' Fees**
Brokers compensation. See **Brokers, Dealers, and Real Estate Salespersons**
California Land Use & Revitalization Act, recovery of expert fees under, 7.32
Finder, recovery of fee by, 2.5
Loan commitment fees, 4.83, 7.89
Preliminary report, fees for, 4.56
Recorder collecting fees prior to recording documents, 15.91
Regulated loans, limits on fees charged for, 2.8
Residential loan modifications, limits on fees for, 2.8B

FEHA. See **Fair Employment and Housing Act (FEHA)**

Fences. See **Boundaries**

Fictitious Business Name
Insuring business under, 14.33

Fiduciary Relationship
Attorneys
Basic duty of, 1.15
Restrictions affecting attorney as fiduciary counsel, 1.7, 1.9
Brokers. See **Brokers, Dealers, and Real Estate Salespersons**
Constructive trust, imposition if title obtained through fraud, mistake, or constructive fraud through violation of fiduciary or confidential relationship, 10.19
Disclosure requirements, exemption for transfers by fiduciary, 6.35
Escrow holder, fiduciary responsibilities of, 15.19
Finder's lack of fiduciary duty to principal, 2.5
Insurers, no claim for breach of fiduciary duty by, 13.121
Mortgage loan broker's fiduciary duty to borrower, 2.8

Financing
See also **Balloon Payments; Due-on-Sale/Encumbrance Clauses; Escrow; Mortgages and Trust Deeds; Promissory Note; Security**
Generally, 9.1
Acceleration of payment. See **Acceleration of Payment**
Amortizing, 4.83, 9.44, 9.62
Appraisals. See **Appraisals and Appraisers**
Arranger of credit, 9.10, 9.13
Attorney's role and standards of care, 9.2-9.5
Buyer's compliance with FIRPTA, 9.23
Cash downpayment, 9.40

Client's risk tolerance, seller financing, 1.51
Commitment, 4.83, 7.89
Construction loan disbursements, 9.80, 9.85
Contingency, 4.3, 4.83
Costs of loan subordination, 9.76
Disclosure of loan charges, 2.8
Disclosure requirements. See **Disclosure**
Environmental report, providing to lender, 7.89
Escrow. See **Escrow**
Federal Truth in Lending Act, 9.13
Fees. See **Fees**
Foreclosure. See **Foreclosure**
Government financing transferability, 9.54
Hotel, effect of relations between lender and manager or franchisor on buyer's financing for purchase of, 5.5
Impound accounts, 4.133, 9.17
Imputed interest obligations, 9.36-9.37
Indemnity, 7.90, 7.92, 7.95
Installment. See **Installment Transactions**
Interest on money. See **Interest on Money**
Land survey requirement, 4.58
Mineral rights reservation recital in deed, effect on obtaining financing, 10.51
Nontraditional and subprime mortgage products, disclosure and compliance requirements for, 2.8A
Options. See **Options**
Original issue discount (OID) obligations, 9.34-9.35, 9.37
Prepayment. See **Prepayment**
Printed loan document, 9.42
Promissory note. See **Promissory Note**
Property insurance protecting lender's interests. See **Property Insurance**
Purchase and sale agreement. See **Purchase and Sale Agreement**
Real Estate Fund. See **Brokers, Dealers, and Real Estate Salespersons**
Refinancing by buyer, 4.38
Releasing parcels from seller's lien as development progresses. See **Releases**
Remediation costs. See **Hazardous Materials and Toxic Waste**
Residential transaction
Computing payments, 9.44
Prepayment of loan or lien, 9.30-9.31, 9.45
Seller financing, 9.6
RESPA. See **Real Estate Settlement Procedures Act (RESPA)**
Secured transactions. See **Secured Transactions**
Securitized loan documents, 4.40
Subordination issues. See **Subordination**
Survey requirements of lender, buyer ascertaining, 4.58
Tax treatment. See **Taxes and Tax Assessments**
Title insurance requirement, 12.3
Usury. See **Usury**
Valuation of property. See **Valuation of Property**
Wraparound financing. See **Mortgages and Trust Deeds**

Finders. See **Brokers, Dealers, and Real Estate Salespersons**

Fines. See **Penalties**

Fires and Fire Protection
California Standard Form Fire Insurance Policy, losses covered under, 13.34
Disclosure of high fire hazard severity zone or wildland fire area, 1.59, 6.48
Party wall, 4.65
Regulated hazardous substances, 7.5

FIRPTA. See **Foreign Investment in Real Property Tax Act (FIRPTA)**

First Refusal, Right of. See **Right of First Refusal**

Fixtures
Residential purchase agreement's default position regarding inclusion of fixtures in sale of real property, 6.8

Floods
See also **Water and Water Rights**
Common law duty to disclose if land subject to flooding, 6.31A
Disclosure of flood hazards, 4.81, 6.48, App N
Insurance
Generally, 13.53
Notice concerning insurance requirements, 6.68

Natural hazard disclosure statement, 4.81, App N
Precontract due diligence, flood zone property, 1.59
Reasonableness test, 4.77

Foreclosure
Generally, 6.106A, 9.22
Antideficiency protection, 4.41, 9.1, 9.8-9.9, 9.55, 9.95-9.99
Attorney purchase of property at foreclosure sale prohibited, 1.7
Bank-owned (REO) sales, 6.110, 6.111
Contaminated property, lender's rights
Generally, 7.88, 7.90
Access, remediation, and receivership rights, 7.94
Survival of indemnities and other agreements after foreclosure, 7.95
Waiver of security, 7.93
Deed in lieu of foreclosure
Generally, 6.106B
Recital in deed, 10.41
Disclosure requirements, exemption for foreclosure sale after default, 6.35
Mechanics' liens, 4.69
Restrictions on foreclosure on owner-occupied residential property, 9.55A
Short sales to avoid foreclosure proceedings. See **Short Sales**
Subrogated rights, 4.42
Title covenants, effect of judicial sale on, 12.22
Wraparound encumbrance default, 9.63-9.64

Foreign Entities
Arbitration, 4.150
Limited partnership, registering with Secretary of State, 4.19, 4.25

Foreign Investment in Real Property Tax Act (FIRPTA)
Certification of nonforeign status by corporation, partnership, trust, or estate, 15.82
Withholding portion of purchase price under
Generally, 9.23, 15.80
Application for withholding certificate, seller's submission of, 15.83
Buyer's obligation to pay withholding amounts, 15.84
California withholding requirements distinguished, 15.84
Certification, App W
Exemptions to withholding requirements, 15.81

Foreign Investors
Applicable laws, review of, 1.85, 1.89

Forfeiture
Buyer's deposit, forfeiture on default, 6.13
Life estate, effect of grant in excess of estate, 10.2
Prisoners' civil rights, 4.18

Franchise Agreements. See **Hotels and Motels**

Fraud and Misrepresentation
"As-is" clause, effect of fraud or misrepresentation on, 6.9
Brokers. See **Brokers, Dealers, and Real Estate Salespersons**
Common law grounds for challenging fraudulent conveyance, 10.13
Constructive trust, imposition if title obtained through fraud, mistake, or constructive fraud through violation of fiduciary or confidential relationship, 10.19
Conveyance without fair consideration, effect on creditors, 10.13
Covenants of title
Effect of fraud invalidating deed, 12.4
Right to convey, effect of false covenant, 12.8
Description of property, fraudulent surveys, 11.93
Escrow. See **Escrow**
Insurance fraud. See **Insurance**
Investigate, effect of buyer's duty to, 6.73
Liability insurance policy, claims for misrepresentation without property damage not covered under, 14.22
Misappropriated funds. See **Misappropriated Funds**
Property insurance. See **Property Insurance**
Purchase and sale agreement. See **Purchase and Sale Agreement**
Statute of frauds. See **Statute of Frauds**
Toxic contamination, failure to give notice to buyer as fraud or misrepresentation, 1.64

Gain or Loss

See also **Risk of Loss**
Different rates for taxing gain from disposition of real property, 1.54
Option contract, capital gain consequences of transferring, 8.37
Recognition of loss, 9.38
Residential purchase and sale transaction, capital gains tax on, 6.97
Tax-deferred exchange, 1.101
Tenancy-in-common transaction to acquire fractional interest in commercial properties, deferring capital gains through, 1.96

Gas. See **Oil and Gas**

General and Specific Plans
Applicable laws, review of, 1.75-1.76

God, Acts of. See **Acts of God or War**

Good Faith and Fair Dealing
Conditional third party approvals as breach of implied covenant of good faith, 3.22
Corporate agent's duty, 4.28
Improvement of lands made in good faith, 11.114
Letters of intent. See **Letters of Intent**
Listing agreement, broker recovering under implied covenant of good faith despite expiration of, 2.52
Misrepresentation of boundary line's location not constituting fraud if seller relies in good faith on misplaced surveyor's mark, 4.59
Property insurance, mutuality of good faith duty between insurer and insured, 13.119
Purchase and sale agreements, 4.3
Purpose of buyer's deposit, demonstrate good faith, 4.37

Governmental Entities. See **Local Government; Public Entities**

Government Surveys. See **Surveys and Surveyors**

Grant Deeds. See **Deeds**

Guaranty. See **Bonds and Undertakings**

Guardianship and Conservatorship
Conveying property for minors and incompetent persons, 4.15-4.17
Deeds, 10.22, 10.24, 10.62

Handicapped Persons. See **Disabled Persons**

Hazardous Materials and Toxic Waste
Agents. See **Agents and Agency**
Agricultural property contamination by pesticides and fertilizers, 7.3
Air quality pollutants, 7.7
Allocation of cleanup or remediation costs
Generally, 7.1, 7.60, 7.74
Private agreement, 7.21
Asbestos-containing materials (ACMs)
Generally, 7.5
Environmental audits, 7.37
Attorney fees
California Land Use & Revitalization Act, attorney fees under, 7.32
CERCLA, attorney fees under, 7.19
Attorney's role in transaction, 1.57, 1.64, 7.1, 7.71
Brownfields statute (see California Land Use & Revitalization Act, below)
Building contaminants
Generally, 7.5
ACMs (see Asbestos-containing materials, above)
Mold (see Mold, below)
Buyer's review of property, 4.80, 4.125, 7.41
Buyer's rights arising from nondisclosed contaminants
Generally, 7.53
Conditions precedent for due diligence, 7.54
De minimus remediation obligation of seller, 7.40, 7.56, 7.57
Indemnity for postclosing discoveries, 7.69, 7.71-7.72
Lessee's estoppel, 7.55
Loan contingency relationship, 7.59
Renegotiating price or other terms, 7.60
Termination rights, 7.58

California Environmental Quality Act (CEQA)
Generally, 1.82, 4.94-4.95, 7.1
Environmental impact report (EIR), 4.95-4.98
Notice of exemptions and negative declarations, 4.96
Statute of limitations for CEQA actions, 4.98
California Land Use & Revitalization Act
Generally, 7.32
Attorney and expert fees under, 7.32
Contribution rights under, 7.32
Immunity from cleanup costs, 7.32
Property under Act, 7.33
Purchasers under Act, 7.34-7.35
Purpose of Act, 7.35
Carpenter-Presley-Tanner Hazardous Substance Account Act (HSA)
Releases and indemnification, 7.61
Scope and purpose, 7.9
Seeking cost recovery from responsible parties, 7.17
CEQA (see California Environmental Quality Act (CEQA), above)
CERCLA (see Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA), below)
Cleanup costs
Allocation of cleanup costs (see Allocation of cleanup or remediation costs, above)
Defenses (see Defenses, below)
Dumpsite cleanup, 7.76
Federal law, 7.8
Insurer's duty to indemnify for damages, exclusion of cleanup costs from, 14.25A
Pollution Legal Liability (PLL) policies, coverage for cleanup costs under, 13.46-13.47, 13.49
Potentially responsible parties' right to bring cost recovery action or pursue contribution claim, 7.17
Private litigant's right to bring clean-up action, restrictions on, 7.17
Remediation costs recovery (see Remediation costs recovery, below)
Seller's CERCLA contribution right against third parties, hazardous substances cleanup agreement between seller and buyer resulting in waiver of, 7.21
State law, 7.9
Comfort letter, 7.77
Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA)
Generally, 1.88, 4.80
Asbestos removal, 7.5
Attorney's fees, recovery under CERCLA, 7.19
Bona fide prospective purchaser defense, 7.22, 7.31, 7.34
Constitutionality of clean up orders under CERCLA, 7.15
Contiguous property owner defense, 7.22, 7.30
Director's and officer's personal liability under, 7.14
Discovery rule for personal injury or property damage under, 7.20
Disposal of toxic contamination, 7.12, 7.25
Equitable defense, unavailability in CERCLA action, 7.22
Indemnification and releases, 7.61, 7.64-7.65
Innocent landowner defense (see Innocent landowner defense, below)
Joint and several liability of owners under, 7.12
Lessees or sublessors, CERCLA "owner" liability on, 7.13
Petroleum exclusion from CERCLA list, 7.8
Petroleum leaks, 7.8
Remediation liability, defenses to, 7.10, 7.22-7.29
Scope and purpose, 7.8
Secured creditor exemption, 7.22, 7.88
Seller's CERCLA contribution right against third parties, hazardous substances cleanup agreement between seller and buyer resulting in waiver of, 7.21
Strict liability, 7.10
Construction and interpretation. See **Construction and Interpretation**
Consultants (see Environmental consultants, below)
Contract provisions
Access to property, 7.85, 7.94
Arbitration clause, 7.84
De minimus remediation costs liability of seller, 7.56, 7.57
Drafting considerations, 7.45, 7.71
Indemnity (see Indemnity, below)
Knowledge of seller, 7.46-7.47, 7.48-7.52
Loan application or documents (see Lender concerns, below)
Private agreement limiting remediation costs liability, 7.21
Releases (see Release from liability, below)
Remediation obligations, generally, 7.73-7.76
Renegotiating terms when undisclosed toxics found, 7.60
Securing remediation costs (see Securing remediation costs, below)
Termination rights, 7.58

Title insurance and searches, 7.86
Controlling law
Federal statutes, 7.8
State statutes, 7.9
Damages
Letter of credit securing liquidated damages, 7.81
Seller's failure to disclose hazardous substances, 7.36
Defenses
Bona fide prospective purchaser defense, 7.22, 7.31, 7.34
CERCLA (see Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA), above)
Contiguous property owner defense, 7.22, 7.30
Innocent landowner defense (see Innocent landowner defense, below)
Remediation defenses (see Remediation defenses, below)
Definitions. See **Definitions**
Disclosure
Buyer's rights (see Buyer's rights arising from nondisclosed contaminants, above)
Due diligence (see Due diligence inquiry and disclosure, below)
Mold, disclosure of, 6.53, 13.130
Representations (see Representations and warranties, buyer's disclosure obligation owed lender; Representations and warranties, seller's disclosure representations, below)
Seller's disclosure of known hazardous substance, 4.49
Underground storage tanks, disclosure of, 6.53
Disposal of contaminants
Innocent landowner defense, 7.25
Liability, 7.11-7.12
Remediation transporters liability, 7.76
Due diligence inquiry and disclosure
Generally, 7.1, 7.87
Buyer's review of property, 7.41
Buyer's rights as to undisclosed contaminants (see Buyer's rights arising from nondisclosed contaminants, above)
Conditions precedent, 7.54
Consultants (see Environmental consultants, below)
Environmental audit reports (see Environmental audit reports, below)
Innocent landowner defense, 7.22, 7.25, 7.86
Leased property, 7.36, 7.55
Lender requirements and time-frame, 7.59, 7.89
Notifying EPA about release of contaminant, 7.43
Seller's knowledge, documenting, 7.46-7.47, 7.48-7.52
Seller's review of property, 7.40
State law, 7.36
Time permitted for investigation, 7.54
Endangered species, 7.1
Environmental audit reports
Attorney-client privilege, 1.64
Consultants, 7.42
Due diligence conditions precedent, 7.54
Lender's receipt, 7.89
Phase I, 7.37
Phase II, 7.38
Remedial investigation/feasibility study/remedial action plan, 7.39
Reviewing before executing agreement, 4.80, 7.45
Environmental consultants
Buyer's use of, 7.41
Confidentiality, 7.43
Principal-agent considerations, 7.44
Scope of work, 7.42
Selection and change of, 7.75
Title chains reviews, 7.37, 7.86
Environmental liability insurance, 7.87
Evidence issues
Bona fide prospective purchaser status, 7.31
Contiguous property owner status, 7.30
Environmental reports as evidence of property condition at closing, 7.72
Innocent landowner status, 7.22, 7.29, 7.86
Fertilizers, 7.3
Foreclosure of liens against contaminated property. See **Foreclosure**
Frequently encountered toxics, 7.2-7.7
Groundwater contamination, 7.4, 7.30-7.31, 7.37
Hazardous Waste Control Law (HCL) of California, scope and purpose, 7.9
Indemnity
Generally, 4.80
Buyer's indemnity of seller, 4.80, 7.69, 7.70, 7.71-7.72

CERCLA and HSA liability, 7.61
Compared to release, 7.66
Covenants of title distinguished from environmental indemnity covenants, 12.1
Lender, 7.90, 7.92, 7.95
Private or separate agreement, 7.21, 7.90
Renegotiating term when undisclosed toxics are found, 7.60
Security (see Securing remediation costs, below)
Seller's indemnity of buyer, 7.67, 7.68
Innocent landowner defense
Generally, 7.12, 7.22, 7.24, 7.86
All appropriate inquiries standards, comparison of, 7.29
Due diligence inquiry and disclosure, 7.22, 7.25, 7.86
Property purchased before May 31, 1997, applicability to, 7.26
Property purchased between May 31, 1997 and November 1, 2006, applicability to, 7.27
Property purchased on or after November 1, 2006, applicability to, 7.28
Qualifying for innocent landowner status, 7.25
Investigation of environmental conditions (see Due diligence inquiry and disclosure, above)
Leased property, 7.36, 7.55
Lender concerns
Generally, 7.90
Access, remediation, and receivership rights, 7.94
Application requirements, 7.89
Assurances on remediation, 7.92
Nature of liability and underwriting, 7.88
Receivership for remediation purposes, 7.94
Representations, 7.91
Rights in foreclosure proceedings. See **Foreclosure**
Secured creditor exemption, 7.22, 7.88
Securing remediation costs (see Securing remediation costs, below)
Survival of indemnities and other agreements after foreclosure, 7.95
Waiver of security interest, 7.93
Mold
Disclosure of, 6.53, 13.130
Landlord's duty to remediate in commercial or industrial property, 4.82
Property insurance coverage, 13.130
Notice
CEQA, notice of exemptions and negative declarations, 4.96
Release of contaminant, notifying EPA about, 7.43
Toxic contamination, notice of, 1.64
Overview on issues, 7.1
Parties liable
Generally, 7.11
Secured creditor exemption, 7.22, 7.88
Transporters, 7.11, 7.14, 7.76
Penalties. See **Penalties**
Permit for disposing of toxic substances, 7.76
Pesticides, 7.3
Polychlorinated biphenyls (PCBs), 7.5
Property insurance coverage against pollution. See **Property Insurance**
Prospective purchaser agreement, 7.77
Proving contamination after close of escrow, 7.72
Purpose of act, 7.35
Release from liability
Generally, 4.80, 7.61
"As-is" clause, 7.64
Broad clause releasing seller, 7.62
Compared to indemnity, 7.66
Expanded "as-is" clause, 7.65
Limited clause releasing seller, 7.63
Remediation costs recovery
Allocation (see Allocation of cleanup or remediation costs, above)
Asbestos-containing materials (ACMs), 7.5
California superfund, restrictions on recovery from, 7.17
Control of process, 7.75
Defenses (see Remediation defenses, below)
Dumpsite cleanup, 7.76
Federal and state law, 7.8-7.9, 7.16
Indemnity (see Indemnity, above)
Private litigant's attorney fees, 7.19
Releases (see Release from liability, above)
Renegotiating contract terms when undisclosed toxics are found, 7.60
Responsibility for costs, 7.74

Secured creditors exemption, 7.22, 7.88
Securing (see Securing remediation costs, below)
Third party issues. See **Third Parties**
Remediation defenses
Generally, 7.22
Allocation and indemnification, 7.1, 7.21
Innocent landowner defense (see Innocent landowner defense, above)
Loan contingency relationship, 7.59
Strict liability under CERCLA, 7.10
Third party defense, 7.22-7.23
Remediation obligations
Generally, 7.1, 7.10, 7.73
Access to property, 7.85, 7.94
Agency assurances, 7.77
Allocation and indemnification agreements, 7.21
Arbitration, 7.84
Assignment of rights, 7.92
Assurances of completion, 7.58, 7.92
Building contaminants, 7.5
California Land Use & Revitalization Act (see California Land Use and Revitalization Act, above)
Comfort letter, 7.77
Control of process, 7.75
Defenses (see Remediation defenses, above)
De minimus obligation of seller, 7.40, 7.56, 7.57
Dumpsite cleanup and disposal of remediation by-products, 7.76
Environmental audit (see Environmental audit reports, above)
Groundwater contaminants, 7.4, 7.30-7.31, 7.37
Hold harmless, 7.21
Issuing abatement or remediation orders, 7.15
Lender concerns (see Lender concerns, above)
Lessees, 7.55
Orders of remediation, 7.15
Parties potentially liable, 7.11, 7.76
Prospective purchaser agreement, 7.77
Receivership, 7.94
Recovery of costs (see Remediation costs recovery, above)
Securing costs (see Securing remediation costs, below)
Soil contaminants, 7.3
Terminology, 7.1
Transporters liability, 7.11, 7.14, 7.76
Reports
Condition of property on closing, environmental reports as evidence of, 7.72
Environmental audit reports (see Environmental audit reports, above)
Representations and warranties, buyer's disclosure obligation owed lender
Generally, 7.91
Survival of indemnities consequences, 7.95
Waiver of security consequences, 7.93
Representations and warranties, seller's disclosure representations
Generally, 7.46-7.47
Absolute representation, 7.49
"As-is" clauses, 7.64, 7.65
Assurances of completing remediation, 7.58, 7.92
Best of knowledge, 7.50
Best of knowledge for specific individuals, 7.51
Best of knowledge with exceptions for Phase I Report, 7.52
Hazardous materials defined, 7.48
Resource Conservation and Recovery Act of 1976 (RCRA), scope and purpose, 7.8
Risks of acquiring contaminated property, review of, 1.64
Sale price, effect on. See **Price**
Secured transactions
Lender concerns (see Lender concerns, above)
Remediation costs (see Securing remediation costs, below)
Securing remediation costs
Generally, 7.78, 7.88
Escrow of funds, 7.60, 7.79, 7.80
Guaranty, 7.82
Letters of credit, 7.81
Offset against buyer's note, 7.83
Seller's review of property
Generally, 7.40
Buyer's resulting rights (see Buyer's rights arising from nondisclosed contaminants, above)
Documenting seller's knowledge, 7.46-7.47, 7.48-7.52

Soil contamination
Generally, 7.3
Groundwater, 7.4, 7.30-7.31, 7.37
Storage tanks, 7.6, 7.9
Storage tanks. See **Storage Tanks**
Superfund (see Carpenter-Presley-Tanner Hazardous Substance Account Act (HSA), above)
Terminology. See **Construction and Interpretation; Definitions**
Third party issues. See **Third Parties**
Time period for Phase I and II investigations, 7.54, 7.59
Title insurance or report, 7.37, 7.86
Transporters liability, 7.76
Waiver
Security interest, waiver of, 7.93
Seller's CERCLA contribution right against third parties, hazardous substances cleanup agreement between seller and buyer resulting in waiver of, 7.21
Warranties (see Representations and warranties, seller's disclosure representations, above)

Health and Safety Standards
Contaminants. See **Hazardous Materials and Toxic Waste**
Disclosure. See **Disclosure**
Fire protection, 7.5

Health Care
Terminated employees, continued health care for, 5.18

Hearings
Brokers. See **Brokers, Dealers, and Real Estate Salespersons**
Federal tax liens, 4.62

Highways. See **Streets, Roads, and Highways**

Historical Background
Early government surveys, misplaced markers, 11.93
Legal description of property. See **Description of Property**
Reservation, creating easement by, 11.73

Hold Harmless
Engineer studies of property, 4.78
Hazardous substances remediation liability, 7.21

Home Equity Sales Contract. See **Residential Purchase and Sale Transactions**

Homeowners' Associations. See **Common Interest Developments**

Homeowners Policies
Liability insurance. See **Liability Insurance for Real Property Transfers**
Property insurance. See **Property Insurance**

Homestead Property
See also **Community or Separate Property**
Acknowledgment of homestead declaration, 15.89
Effect of declaration of homestead, 10.57
Purchase and sale, 4.19

Hotels and Motels
Generally, 5.1
Associated resort facilities, hotel's relationship with, 5.6
Closing conditions
Generally, 5.20
Bulk sales laws, compliance with, 5.23
Form, 5.25
Franchisor and manager, required actions by, 5.21
Liquor license, transfer of, 5.22
Material adverse changes prohibited, 5.24
Safe deposit and baggage, 5.28
Due diligence (see Purchase and sale agreement for hotel, below)
Escrow and closing
Conditions for closing (see Closing conditions, above)
Form, 5.29
Inventories (see Inventories, below)
Liquor license, escrow for transfer of, 5.27
Prorations, 5.26

Estoppel certificate from hotel operator, App R
Franchise agreements (see Referral, management, and franchise agreements for operation of hotel, below)
Inventories
Consumables and expendables, inventory of, 5.26
Contents of safe deposit boxes and baggage check facilities, inventory of, 5.28
Liquor license
Closing condition, transfer of liquor license as, 5.22
Escrow for transfer of, 5.27
Long-term residents, facilities for, 5.7
Management of property (see Referral, management, and franchise agreements for operation of hotel, below)
Purchase and sale agreement for hotel
Assets and liabilities, 5.10, 5.11
Closing conditions (see Closing conditions, above)
Definitions, 5.9
Due diligence documents, 5.13
Due diligence of buyer, 5.12
Employees, 5.18, 5.19
Escrow (see Escrow and closing, above)
Form, App Q
Nature of hotel operations, agreement reflecting, 5.2
Preclosing covenants, 5.14, 5.15
Representations and warranties by seller, 5.16, 5.17
Terminology, 5.8
Referral, management, and franchise agreements for operation of hotel
Generally, 5.3
Buyer's financing for purchase of hotel, effect of relations between lender and manager or franchisor on, 5.5
Closing conditions, required actions by franchisor and manager, 5.21
Issues affecting franchise or management agreements, 5.4
Residential and common interest arrangements, 5.7
Sales tax on sale of hotel's personal property, 5.29

Husband and Wife. See **Marital Relationships**

Immunity
California Land Use & Revitalization Act, immunity from cleanup costs under, 7.32

Implied Covenants. See **Covenants**

Implied Warranties
New home construction, implied warranties limited to, 6.30

Impound Accounts. See **Escrow**

Improvements and Repairs. See **Construction, Improvements, and Repairs**

Income-Producing Property
See also **Investments; Leases; Rents**
Hotel purchase and sale agreement, provision for proration of income and expenses, 5.26

Income Tax. See **Taxes and Tax Assessments**

Incompetent Persons
Generally, 4.16-4.17
Deed to incompetent person, 10.24, 10.26

Incorporation by Reference
Deeds, exhibits and riders, 10.36, 10.38
Description of property, 4.31

Indemnity
See also **Releases**
Access license and indemnity agreement, App P
Attorney's fees, indemnity agreement providing for, 7.66
Brokers
Principal's right to indemnity for damages recovered by third parties for broker's actions, 2.163
Seller's misrepresentations, seller's indemnification of broker for, 2.183
Buyer's onsite investigation and tests, 4.48, 4.78
Consultants' form contracts, overly protective indemnity provisions in, 1.69
Encumbrances, covenant against as promise to indemnify, 12.7
Environmental, 4.80
Foreclosure, survival of indemnities and other agreements after, 7.95

Independent contractor's lack of entitlement to indemnification by employer, 2.20
Liability insurance. See **Liability Insurance for Real Property Transfers**
Limited liability company members, 4.27
Property insurance. See **Property Insurance**
Release and indemnity compared, 7.66
Remediation costs. See **Hazardous Materials and Toxic Waste**
Seller seeking indemnity from assuming grantee, 4.41
Simultaneous exchange, buyer's indemnity, 4.127
Testing on property, 4.48, 4.78
Third parties. See **Third Parties**
Title policies, negotiating exceptions and indemnities, 11.13, 11.75

Independent Contractors
Indemnification from employer, independent contractor's lack of right to, 2.20
Salesperson as independent contractor for real estate broker, 2.15-2.16, 2.19

Independent Escrow Companies. See **Escrow**

Inferences. See **Presumptions and Inferences**

Inheritance
Contaminated property remediation liability, 7.22

Injunctions
Commissioner of Corporations seeking injunction against escrow company, 15.4
Easements, termination by incompatible use or misuse, 11.61
General plan, local approval enjoined for inconsistency with, 1.76
Hazardous substances, remediation order, 7.15

Insolvency. See **Bankruptcy and Insolvency**

Inspection of Property
Generally, 6.75
Boundary disputes, inspection of residential property for evidence of possible, 6.7
Buyer, inspection by
Conditional sales agreement requiring seller to make documents regarding property accessible for buyers inspection, 4.48
Due diligence, buyer's inspection of property as part of, 6.74
Early access for buyer's inspections, 3.41
Inspection advisory (CAR Form BIA), 6.25
Defects in title, inspection as part of bona fide purchase defense, 11.75
Description of property, 11.11
Engineering studies, 4.77-4.78
Environmental issues. See **Hazardous Materials and Toxic Waste**
Facts material to buyer, no duty on seller to inspect property or investigate, 6.30
FHA/HUD inspection disclosure, 6.67
Home inspection, 6.77
Knowledge and experience of seller or purchaser, effect on scope of investigations, 1.55-1.56
Notice
Buyer's notice of matters discoverable by inspection, 11.11
Constructive notice, inspection of property as, 11.11
Constructive notice of matters discoverable by inspection, 4.70
Off-record easements, 11.53
Pest inspection. See **Pests and Pest Control**
Question of fact, discoverability of defect on inspection as, 4.49
Seller presale due-diligence matters, other investigations needed, 1.63
Soil tests, 4.77
Suitability of physical condition of property. See **Purchase and Sale Agreement**
Surveys. See **Surveys and Surveyors**
Water, effect on description of property, 11.111

Installment Transactions
Acceleration of payment. See **Acceleration of Payment**
Disposition of installment obligations, 9.33
Due-on-sale/encumbrance. See **Due-on-Sale/Encumbrance Clauses**
Escrow. See **Escrow**
Land contract
Generally, 9.14
Disadvantages and decline in popularity, 9.16
Misappropriation of funds for installment land contract payments, 9.63
Promissory note secured by mortgage or trust deed distinguished, 9.22
Protective statutory and legal provisions, 9.17
Purchase and sale agreement distinguished, 9.15

Mortgages. See **Mortgages and Trust Deeds**
Option agreement characterized as installment sale, income tax consequences of, 8.35
Personal property being transferred with real property, installment payments on, 4.133
Prepayments. See **Prepayment**
Releasing parcels from seller's lien as property developed. See **Releases**
Segregated parcels, 4.133
Subordination. See **Subordination**
Taxes. See **Taxes and Tax Assessments**
Withholding requirements for installment sales. See **Escrow**

Instructions for Escrow. See **Escrow Instructions**

Insurance
Brokers, errors and omissions insurance for. See **Brokers, Dealers, and Real Estate Salespersons**
Casualty insurance, 4.139
Certificate of insurance
Liability insurance, certificate of insurance for additional insured, 14.41
Property insurance, certificate of insurance not constituting contract between insurer and certificate holder, 13.23
Confirmation of property's insurability by buyer, 6.74
Consumer Legal Remedies Act allowing private right of action for unfair or deceptive practices, inapplicability to insurance, 13.123
Earthquake insurance. See **Earthquakes and Seismic Activity**
Endorsements
Liability insurance endorsements for additional insureds. See **Liability Insurance for Real Property Transfers**
Property insurance, endorsement defining remedial plan for cleanup of pollutants, 13.49
Title insurance. See **Title Insurance and Preliminary Report**
Environmental liability insurance, 7.87
Escrow
Closing escrow, 4.106, 4.139, 4.172
Exemption of insurance companies from escrow law, 15.6
Proration of insurance premiums, 15.45
Evidence
Liability insurance. See **Liability Insurance for Real Property Transfers**
Property insurance, certificate of insurance as evidence of, 13.23
Exclusions
Liability insurance. See **Liability Insurance for Real Property Transfers**
Mold, 13.130
Property insurance. See **Property Insurance**
Residential title insurance policies, exceptions and exclusions, 6.84
Flood insurance. See **Floods**
Fraud
Property insurance policy, fraud as grounds for reformation of, 13.25
Title insurance, negligent error or misrepresentations, 11.13
Hazard insurance, 7.87
Liability insurance. See **Liability Insurance for Real Property Transfers**
Premiums, proration of, 4.133, 15.45
Professional liability insurance, attorney's required disclosure regarding, 1.12A
Property insurance. See **Property Insurance**
Purchase and sale agreement, cancellation or assumption of insurance, 4.106, 4.139, 4.172
Terrorism. See **Terrorism**
Title insurance. See **Title Insurance and Preliminary Report**
Unemployment insurance system, exclusion of brokers and real estate salespersons from, 2.17
Workers' compensation, applicability to salespersons, 2.18

Intangible Property
See also **Personal Property**
Assignment agreement, App J
Describing intangible property included in sale, 4.34

Intent
Abandonment, 11.80
Ambiguity, effect on ascertaining parties' intent, 4.8
"As-is" clauses, 7.64
Corporation's acceptance of deed, evidence of intent, 10.75
Covenants merged in deed, proof of contrary intent, 12.4
Delivery of deed, intent to transfer title requirement, 10.71-10.72
Description of property
Generally, 11.14-11.15
Exception and reservation, distinguishing by parties' intent, 11.73
Monument doctrine, presumption of intent, 11.31
Multiple parcels, 11.109
Streets and public rights-of-way, construing grant to center of highway absent other intent, 11.30

Easements. See **Easements**
Implied intent to dedicate by grant of license, 11.77
Letters of intent. See **Letters of Intent**
Physical condition of property, determining suitability for buyer's intended use. See **Purchase and Sale Agreement**
Signatures to agreement, 4.12

Interest on Money
Breach of insurance contract, recovery of prejudgment interest, 13.113
Buyer's financing commitment, 4.83
Computation, 9.44
Covenants of title, recovery of interest on breach, 12.19
Escrow deposits, 4.37, 4.170, 15.37
Original issue discount and imputed interest obligations, 9.34-9.37
Prorating in property sale transaction, 4.133
Usury. See **Usury**
Wraparound financing, 9.7, 9.57-9.58

Interests in Property
Easements. See **Easements**
Equity interests. See **Equity Interests**
Fee interest. See **Fee Interest**
Joint tenancy. See **Joint Tenancy**
Life estates. See **Life Estates**
Reconveyances and releases. See **Releases**
Tenancy-in-common. See **Tenancy-in-Common**

Interference with Prospective Economic Advantage. See **Brokers, Dealers, and Real Estate Salespersons**

Internet
See also **Computers**
Definition of Internet escrow agent, 15.5

Interpleader
Escrow holder filing, 15.97-15.98

Interpretation of Cases and Statutes. See **Construction and Interpretation**

Inventory
Hotel purchase and sale agreement, inventory provisions. See **Hotels and Motels**
Personal property transferred with real property, description of, 11.97, 11.118
Property insurance, value reporting clauses regarding inventory, 13.111

Investigations
See also **Due Diligence**
Broker's breach of duty of care in failing to advise client to investigate title matters, 2.144
Buyer's duty to investigate, 6.73
Buyer's onsite investigation and tests, 4.48, 4.78
Contaminated property. See **Hazardous Materials and Toxic Waste**
Facts material to buyer, no duty on seller to inspect property or investigate, 6.30
Inspection and testing of property. See **Inspection of Property**
Liability insurance, insurer's duty to provide investigative expenses as part of duty to defend, 14.14
Option contract, investigation of property as part of. See **Options**
Property insurance claim, insured's duty to cooperate with insurer's investigation of, 13.90
Purchase and sale agreement, approval of onsite investigation and tests, 4.78
Reliance on seller's representation of fact, buyer's justification in, 6.73
Value of property, buyer's right to investigate conditions affecting, 6.74

Investments
See also **Income-Producing Property; Rents**
Dealer property distinguished, 9.32
Foreign Investment in Real Property Tax Act (FIRTA) withholding liability, 9.23

Joint and Several Liability
Broker's misrepresentations to buyer, broker's and seller's joint and several liability for, 2.183
CERCLA, owners' joint and several liability under, 7.12

Joint Tenancy
See also **Tenancy-in-Common**
Generally, 6.87
Community property. See **Community or Separate Property**
Consent

Deeds, consent to joint tenancy between one spouse and another person, 10.40
Severance of joint tenancy without consent of other joint tenants, 10.58
Death of joint tenant
Generally, 4.22
Vesting title in survivor, 4.19
Deeds
Changing title from joint tenancy to community property, grantee recital, 10.34
Closing conditions involving multiple sellers, 4.128
Consent to joint tenancy between one spouse and another person, 10.40
Grantee recitals, 10.31
Termination of, 10.58
Partition, 4.23
Tenancy-in-common distinguished, 4.22
Termination, 4.22, 6.87, 10.58
Title requirements, 4.19

Joint Ventures
Broker receiving commission if property conveyed to, 2.98
Defective limited partnerships, 4.25
Grantor recitals in deed, 10.21
Signature on deed, 10.66

Judgments
Breach of covenant against encumbrances, judgment liens, 12.14
Brokerage industry. See **Brokers, Dealers, and Real Estate Salespersons**

Judicial Sale. See **Foreclosure**

Laches
See also **Statutes of Limitations**
CERCLA actions, unavailability of laches defense in, 7.22

Landlords. See **Leases; Rent**

Landslides and Subsidence
See also **Earthquakes and Seismic Activity**
Common law duty to disclose prior landslides, 6.31A-6.32
Exclusions from property insurance for damage caused by earth movement, 13.87

Land Use
See also **Zoning**
Condemnation and eminent domain. See **Condemnation and Eminent Domain**
Developers. See **Developers**
Option contract, using for land use development. See **Options**

Lead-Based Paint
Disclosure of lead-based paint to residential buyer, 6.51

Leases
See also **Income-Producing Property; Rent**
Agricultural leases, 4.74
Assignment, 4.73, 4.75, 8.57, App I
Attorney's review of leases, 4.71-4.73
CERCLA "owner" liability on lessees or sublessors, 7.13
Deeds
Cloud on title, deed subject to lease with option to purchase as, 12.23
Termination of recorded lease, 10.48
Description of property, forms of ownership, 11.5
Disclosure of hazardous substances released on or under lease, 7.36, 7.55
Due diligence checklist, materials seller delivers to buyer in sales involving commercial leases, App B
Escrow instructions concerning transfer of lease from seller to buyer, 15.39
Ground leases, 4.75
Hotel equipment, 5.10
Insurable interest under lease, 13.20
Letter of intent regarding lease execution, 3.19
Listing agreement giving broker right to commission on lease or exchange of property, 2.98
Marketability of title consequences. See **Purchase and Sale Agreement**
Mold in commercial or industrial property, landlord's duty to remediate, 4.82
Option to purchase in lease
Generally, 8.57
Acknowledgment as condition for recording, 10.46

Assignability of option contract for purchase of real property, 8.25, 8.70
Deed subject to lease with option as cloud on title, 12.23
Distinguishing from hidden security device, 9.20-9.21
Hidden security device, 9.19-9.21
Promissory note secured by mortgage or trust deed distinguished, 9.22
Reasons to use, 9.18
Tax treatment, 9.20-9.21
Tenant's right to purchase, 4.3
Purchase and sale agreement. See **Purchase and Sale Agreement**
Purchaser's alternative, leasing transaction as, 1.34
Recordation of, 9.18, 10.46
Removal of tenants, 4.72, 4.74, 4.103, 4.136
Seller's alternative, leasing transaction as, 1.27
Statute of frauds, 10.1
Subleasing restrictions, 4.75
Tenant's estoppel certificate, 4.73, 4.101, 12.7, 15.39, App K
Termination of tenant's lease, 4.72, 4.74, 4.103, 4.136, 10.48

Legal Ethics
Generally, 1.3
Rules of Professional Conduct
Generally, 1.4
Attorney's own interest, conflict, 1.7
Client's property, handling, 1.12
Competence defined, 1.5
Conflicts of interest, 1.6-1.11
Financial relationships, rules governing, 1.6
Informed written consent, 1.10
Legal opinions, standards for preparing, 1.126
Multiple representation, 1.11
Other interests, conflicts with, 1.8-1.11
Standard of performance, 1.5
Written disclosure requirements, 1.9

Legal Malpractice
Generally, 1.3, 1.13, 9.4-9.5
Duty of care, 1.14
Resource materials on malpractice, 1.16
Seller financing aspect of transaction, 9.4-9.5

Legal Opinions
Generally, 1.121
Recognizing legal opinions
Avoiding unnecessary opinions, 1.125
Factual, reasoned, or comfort opinion, 1.124
Statement of knowledge as legal opinion, 1.122
Writing construed as legal opinion, 1.123
Resources available
Generally, 1.127
ABA reports, 1.129
Accord, 1.130
State bar reports, 1.128
Standards for preparing, 1.126
Structuring buyer, attorney's opinion regarding, 9.3

Lenders. See **Financing**

Letters of Credit
Deposit method in purchase and sale transaction, 4.37, 4.170
Remediation costs payment security, 7.81

Letters of Intent
Attorney-written letter or letter prepared without legal assistance, 3.3-3.4
Binding agreement on certain matters, creation of, 3.11
Binding or nonbinding letter, determining use of, 3.13, 3.35
Competing offers, agreement not to solicit, 3.11
Damages
Generally, 3.26, 3.30
Liquidated damages provision in, 3.12, 3.15, 3.30, 3.35
Deal-breaker issues, identification of, 3.8
Defined, 3.1
Detrimental reliance on, 3.3, 3.14, 3.26

Drafting
Buyer's contingencies, 3.40
Commissions, 3.44
Confidentiality, 3.45
Deposits, 3.38
Description of property, 3.36
Early access for inspections, 3.41
Escrow, 3.43
Execution of letter of intent, 3.19, 3.24, 3.46
Heading, 3.33
Introductory clause, 3.34
Parties intentions on binding or nonbinding nature, 3.35
Purchase and sale agreement, 3.39
Purchase price and payment of, 3.37
Seller's representations and warranties, 3.42
Enforceability unintended, 3.15, 3.19, 3.24
Estoppel, 3.10, 3.14, 3.26
Evidence
Contract formation, evidence of, 3.16-3.17
Extrinsic evidence to determine binding effect of letter, effect of requiring, 3.26
Execution of, 3.19, 3.24, 3.46
Good faith
Conditional third party approvals as breach of implied covenant of good faith and fair dealing, 3.22
Duty to negotiate in, 3.11, 3.27-3.30, 3.35
Intent, determining
Generally, 3.17
Complexity and size of proposed transaction, 3.23
Future execution of contract clause, effect of, 3.19
Language choice and verb tense, effect on intent, 3.20
Parties' conduct, 3.18
Specificity of essential terms as indicative of intent, 3.21
Statute of frauds, 3.25-3.26
Texaco v Penzoil, unexpected enforceability, 3.24
Third party approvals, 3.22
Limited use of letter of intent for seller, 1.102
Liquidated damages provision in letter of intent, 3.12, 3.15, 3.30, 3.35
Miscellaneous considerations, 3.47
Mutual assent, objective manifestation of, 3.16
Negotiation
Drafting letter as negotiating advantage, 3.31
Effect of, 3.9
Good faith duty, 3.11, 3.27-3.30, 3.35
Partial performance, reduction of risks, 3.10
Risks of, 3.14-3.16
Specific performance, 3.13-3.14
Structuring transactions, method of, 3.7
Time, cost, and efficiency issues, 3.6, 3.11
Use of and purpose of, 3.2, 3.5
Waiver, 3.10, 3.14, 3.24

Liability Insurance for Real Property Transfers
Generally, 14.1
Accident (see Occurrence or accident in commercial general liability (CGL) policies, below)
Additional insured
Generally, 14.37
Certificate of insurance, 14.41
Defined, 14.37
Duty to defend, effect of restrictions on coverage of additional insured on, 14.39
Endorsements (see Endorsements for additional insureds, below)
Named insured (see Named insured, below)
Notice of cancellation, additional insureds not entitled to, 14.37
Rights of additional insureds under policy, 14.37
Statutory limit on indemnity provisions, 14.40
Advertising injury (see Personal and advertising injury, below)
Bodily injury
Generally, 14.28
Additional insured, restrictions on bodily injury coverage for, 14.37
Emotional distress with or without physical injury, 14.29-14.30
Stated policy period (see Stated policy period, effect on coverage, below)
Claims made and reported policies, 14.14-14.14A
Claims made policies
Generally, 14.13

Distinction between occurrence-based policy and claims made policy, 14.12
Extending reporting period under, 14.15
Retroactive date, claims made policies containing, 14.16
Commercial general liability (CGL) insurance
Generally, 14.3, 14.17
Bodily injury (see Bodily injury, above)
Contractual indemnity obligations assumed by insured, CGL policy not covering, 14.51
Duties of insurer under, 14.17
Duty to defend (see Duty to defend, below)
Economic damages, elimination of coverage for, 14.25
Exclusions (see Exclusions, below)
Insured parties (see Parties insured under commercial general liability (CGL) insurance, below)
Occurrence or accident (see Occurrence or accident in commercial general liability (CGL) policies, below)
Personal and advertising injury (see Personal and advertising injury, below)
Products or completed operations hazard defined, 14.57
Property damage (see Property damage under commercial general liability policy, below)
Stated policy period (see Stated policy period, effect on coverage, below)
Costs
Allocation of indemnification costs among multiple insurers, 14.48
Damages, attorney fees and costs included within definition of, 14.51
Reimbursement of defense costs, insurer seeking for claims not potentially covered, 14.56
Defend, duty to (see Duty to defend, below)
Duty to defend
Generally, 14.52
Additional insureds, effect of restrictions on coverage on insurer's duty to defend, 14.39
Burden on insurer to establish no duty to defend, 14.37
Comprehensive or commercial general liability insurance policies, insurer's duty to defend under, 14.17
Continuous or progressively deteriorating damage or injury, duty of multiple insurers to defend all parts of claim, 14.48
Entire claim, duty to defend extending to, 14.54
Extrinsic evidence supporting duty to defend, 14.55
Indemnify, duty to defend broader than duty to, 14.53
Investigative expenses, insurer's duty to provide as part of duty to defend, 14.14
Property acquired by insured after policy period stated in policy, insurer's lack of duty to defend insured for claims relating to, 14.50
Refusal to defend insured, determining reprehensibility of conduct for purposes of punitive damages, 13.118A
Reimbursement of defense costs, insurer seeking for claims not potentially covered, 14.56
Endorsements for additional insureds
Generally, 14.42
Acts or omissions of named insured, additional insurance endorsement referring to, 14.45
"Arising out of" versus "caused, in whole or in part, by" endorsement, 14.43
Manuscript additional insured endorsements, 14.46
Ongoing operations, 14.44
Sole negligence of additional insured, endorsement covering, 14.38
Environmental liability insurance, 7.87
Evidence
Certificate of insurance as evidence of liability insurance, 14.41
Duty to defend, extrinsic evidence supporting, 14.55
Exclusions
Businessowners policy, 14.71
Homeowners policy (see Homeowners policy, below)
Negligent construction or design, 14.24
Personal and advertising injury, exclusions for, 14.70
Property damage exclusions (see Property damage exclusions, below)
Real estate agents' errors and omissions liability policy, exclusions in, 14.75
Representations and warranties liability insurance, exclusions affecting, 14.79
"The insured", "an insured", or "any insured", exclusions referring to, 14.35
Faulty workmanship exclusion
Generally, 14.64
Distinction between damage to building caused by removal of defective materials and faulty workmanship, 14.65
Homeowners policy
Generally, 14.10
Arising out of the sale exclusion, 14.85
Business exclusion, 14.82
Insuring language, 14.80
Noninsured location, exclusion affecting, 14.84
Professional services exclusion, 14.83
Indemnification
Additional insured, statutory limit on indemnity provisions, 14.40
Allocation of indemnification costs among multiple insurers, 14.48
Commercial general liability (CGL) insurance policy not covering contractual indemnity obligations assumed by insured, 14.51
Duty to defend broader than duty to indemnify, 14.53
Property acquired by insured after policy period stated in policy, insurer's lack of duty to indemnify or defend insured for

claims relating to, 14.50
Insurance Services Office (ISO) versus manuscript policies, 14.2
Interpretations
Distinction between "arising out of" versus "caused, in whole or in part, by" endorsements, 14.43
"The insured", "an insured", or "any insured", interpretation of, 14.35
Issues arising under various policies, 14.11
Malpractice insurance for real estate agents. See **Brokers, Dealers, and Real Estate Salespersons**
Named insured
Generally, 14.32
Additional named insureds, 14.36
Additional named insured's right to notice of cancellation, 14.37
Distinguishing additional insured from named insured, 14.32, 14.37
Exclusions referring to "the insured", "an insured", or "any insured," 14.35
Fictitious name, insuring business under, 14.33
Partners and spouses as additional insureds, 14.34
Occurrence or accident in commercial general liability (CGL) policies
Claims for negligent or intentional misrepresentation or concealment without including property damage, no coverage under CGL policy, 14.22
Definitions, 14.18
Examples of accidental conduct, 14.20
Examples of non-accidental conduct, 14.21
Latent defects, 14.23
Negligent and accidental as nonsynonymous terms, 14.19
Occurrence policies, 14.12
Parties insured under commercial general liability (CGL) insurance
Generally, 14.31
Additional insured (see Additional insured, above)
Named insured (see Named insured, above)
Personal and advertising injury
Generally, 14.69
Exclusions, 14.70
Property damage exclusions
Generally, 14.58
Alienated premises exclusion, 14.60
Faulty workmanship (see Faulty workmanship exclusion, above)
Impaired property, damage to, 14.68
Loaned property, exclusion for, 14.61
Money damages, insurer's duty to indemnify limited to, 14.25A
Personal property in care, custody, or control of insured, exclusion eliminating property damage for, 14.62
Pollution exclusion, 14.68A
Product exclusion, 14.66
Property owned, rented, or occupied by insured, exclusion for property damage to, 14.59
Work completed exclusion, 14.67
Work performed by or on behalf of named insured, exclusion for, 14.63
Property damage under commercial general liability (CGL) policy
Generally, 14.25
Physical injury to other property, 14.26-14.27
Stated policy period (see Stated policy period, effect on coverage, below)
Representations and warranties liability insurance
Generally, 14.9, 14.76
Claims made basis, coverage on, 14.78
Exclusions, 14.79
Insuring language, 14.77
Stated policy period, effect on coverage
Generally, 14.47
Continuous or progressive property damage, 14.48
Examples of continuous and progressive damage, 14.49
Known injury or damage provision in post-1998 ISO CGL policies, 14.49A-14.49C
Number of occurrences, determination of, 14.49D
Property acquired by insured after policy period stated in policy, insurer's lack of duty to indemnify or defend insured for claims relating to, 14.50
Trigger activating insurer's duty to defend, 14.47
Types of liability insurance
Architects and engineers professional liability policy, 14.6
Businessowners liability policy, 14.4, 14.71
Commercial general liability insurance (see Commercial general liability (CGL) insurance, above)
Contractors Professional Liability policy, 14.7
Homeowners policy (see Homeowners policy, above)
Owners and contractor protective policy, 14.5
Real estate agent's errors and omissions policy, 14.8
Representations and warranties insurance (see Representations and warranties liability insurance, above)
Warranties (see Representations and warranties liability insurance, above)

Licensed Care Facility
Duty to disclose existence of licensed care facility serving more than six persons in neighborhood, 6.33

Licenses and Permits
Access license and indemnity agreement, App P
Brokers and salespersons. See **Brokers, Dealers, and Real Estate Salespersons**
Building permit, 1.79, 1.84, 4.86, 4.89
Coastal development permit, 4.88
Conditional use permits and variances, 4.87
Escrow company. See **Escrow**
Liquor license, transfer of. See **Hotels and Motels**
Option agreement, provision dealing with governmental permits, 8.69
Partner as real estate licensee, 2.4
Storage tanks, 7.6
Structural Pest Control Board, 4.79
Toxic substances cleanup disposal permit, 7.76

License To Use Property
Covenant of seisin, effect of license, 12.13
Easement by necessity, 11.56
Implied intent to dedicate by grant of license, 11.77

Liens and Encumbrances
Antideficiency protection, limits on applicability if seller secures purchase price with lien on different piece of property, 9.9
Assessments. See **Taxes and Tax Assessments**
Buyer taking encumbered property. See **Purchase and Sale Agreement**
Covenant against encumbrances. See **Covenants of Title**
Damages for breach of covenant against encumbrances, 12.14
Due-on-sale clause, 4.43
Duty owed junior lienholder, 9.88
Easements. See **Easements**
Installment land contract, failure to apply payments to existing encumbrance, 9.63
Mechanics' liens. See **Mechanics' Liens**
Mortgages and trust deeds. See **Mortgages and Trust Deeds**
Option's priority over encumbrance acquired after date of initial option, 8.22
Secured transactions. See **Secured Transactions**
Subordination. See **Subordination**
Superiority of tax liens over earlier recorded private liens, 4.60
Tax liens. See **Taxes and Tax Assessments**
Title review by buyer, review of liens as part of, 6.80
Title, taking subject to existing encumbrance, 4.38
Wraparound encumbrance default, 9.63-9.64

Life Estates
Description of property, forms of ownership, 11.5
Excepting or reserving language in deed to convey, 11.73
Grant in excess of estate, 10.2
Insurable interest in property, life tenant and remainderman having, 13.16, 13.21A
Recital in deed, 10.52

Like-Kind Exchanges. See **Exchange of Property**

Limitation of Actions. See **Statutes of Limitations**

Limited Liability Company (LLC)
Generally, 4.20, 4.27
Certificate authorizing execution of documents required for real property purchase, App E

Limited Liability Partnership. See **Partnerships**

Limited Partnerships. See **Partnerships**

Liquidated Damages
Attorney reviewing enforceability of liquidated damages clauses, 1.99
Deposit, seller's right to retain as liquidate damages, 2.119
Enforceability problems, 4.142
Format and amount restrictions, 4.37, 4.141
Letter of credit securing liquidated damages, 7.81
Letter of intent, liquidated damages provision in, 3.12, 3.15, 3.30, 3.35
Option contract as substitute for, 8.39
Purchase and sale agreements, 2.119, 4.140-4.143, 4.149

Remediation costs, 7.81
Residential purchase and sale transactions. See **Residential Purchase and Sale Transactions**
Structuring transaction, 1.99

Liquidation
Commissioner of Corporations seeking liquidation of escrow company for violation of escrow law, 15.4

Liquor License, Transfer of. See **Hotels and Motels**

Lis Pendens
Letters of intent, 3.13-3.14
Recorded notice of lis pendens, 4.116

Listing Agreement
See also **Brokers, Dealers, and Real Estate Salespersons**
Generally, 2.54
Buyer's deposit, provisions for
Authority to accept deposits, 2.68
Broker holding buyer's deposit, 2.67
Handlings deposits, 2.69, 2.70
Payment of broker from seller's deposit, 2.78
Checklist, 2.55
Compensation of broker, provisions for
Generally, 2.92
Amount of commission, listing agreement setting, 2.118
Buyers excluded from agency agreement, 2.80
Closing, broker's commission not conditioned on, 2.77
Closing, payment of commission conditioned on, 2.76
Conditions (see Conditions for broker's commission, below)
Deposit, payment of broker from, 2.78
Drafting considerations, 4.135
Entitlement of broker to commission, 2.79
Failure to deliver copy of listing agreement, effect on broker's right to commission, 2.88
Net listing arrangement, broker's commission under, 2.61
Procuring cause of sale, commission dependent on broker being, 2.92, 2.103
Rights and duties of broker, listing agreement governing, 2.97
Safety clause (see Safety clause for broker's commission, below)
Sale after termination of listing period (see Sale after termination of listing period, broker's recovery of commission, below)
Sharing of compensation by brokers, 2.93
Transaction other than outright sale, provision giving broker right to commission, 2.98
Conditions for broker's commission
Generally, 2.110
Examples of conditions, 2.111
Real estate residential purchase agreement and receipt for deposit, conditions created by, 2.113
Residential exclusive authorization and right to sell, effect of safety clause in, 2.112
Defined, 2.54
Deposits, provisions for (see Buyer's deposit, provisions for, above)
Drafting considerations, broker's right to commission, 4.135
Duties of broker, provisions for
Generally, 2.83
Due diligence in performance of duties, effect of broker failing to exercise, 2.83
Form, broker's duties, 2.84
Exclusive agency
Generally, 2.58
Commission for broker, effect of seller being procuring cause of transaction, 2.92, 2.103
Revocation of exclusive agency, broker's lack of diligence as grounds for, 2.148
Exclusive right to sell listing
Generally, 2.56
Commission, broker's right to, 2.92, 2.103
Residential listing agreement (exclusive authorization and right to sell, CAR Form RLA), 2.57
Revocation of exclusive agency, broker's lack of diligence as grounds for, 2.148
Safety clause (see Safety clause for broker's commission, below)
Expiration of listing agreement, broker recovering under implied covenant of good faith, 2.52
Extent of broker's authority to bind principal, listing agreement specifying, 2.42
Format and provisions for
Generally, 2.62
Acceptance of agreement by broker, 2.88
Acknowledgment of receipt by seller, 2.88
Arbitration clause, 2.85
Broker cooperation, submission of listing to multiple listing service, 2.75
Buyer's deposit (see Buyer's deposit, provisions for, above)
Compensation of broker (see Compensation of broker, provisions for, above)

Duties of broker (see Duties of broker, provisions for, above)
Escrow holder, selection of, 2.71, 2.72
Execution of agreement, 2.86
Indemnity provision, 2.183
Listing price (see Listing price, below)
Possession of property at close of escrow, 2.73
Printed form subordinate to drafted provisions, 2.87
Safety clause (see Safety clause for broker's commission, below)
Termination date (see Termination date, below)
Listing price
Form, listing price, 2.66
Negotiating listing price, 2.65
MLS issues. See **Multiple Listing Services (MLS)**
Net listing arrangements, potential for abuse, 2.61
Notice required of seller. See **Notice and Notification**
Open listing
Generally, 2.59
Nonexclusive (open) agency residential listing agreement (authorization and right to sell, CAR Form RLAN), 2.60
Procuring cause of contact between seller and buyer, commission dependent on broker being, 2.92, 2.103
Oral modification of, 2.53
Safety clause for broker's commission
Generally, 2.56, 2.81
Procuring cause of sale, broker as, 2.105
Residential exclusive authorization and right to sell, effect of safety clause in, 2.112
Sale after termination of listing agreement (safety clause), 2.82, 2.116
Sale after termination of listing period, broker's recovery of commission
Generally, 2.115
Safety clause, recovery under, 2.82, 2.116
Statute of frauds prohibiting recovery of commission if broker procures buyer after expiration of listing agreement, 2.115
Two commissions, seller's liability for, 2.117
Statute of frauds issues. See **Statute of Frauds**
Strict construction of agreement against broker, 2.56
Termination date
Exclusive right-to-sell agreement without definite termination date, disciplinary action against broker trying to recover compensation under, 2.56
Listing period, 2.64
Need for definite termination date, 2.63
Termination of listing
Broker's right to commission, effect of terminating agreement on, 2.105
Due diligence in performance of duties, broker's failure to exercise as grounds for owner's revocation of listing, 2.83
Safety clause (see Safety clause for broker's commission, above)
Sale after termination of listing period (see Sale after termination of listing period, broker's recovery of commission, above)
Types of listing agreements
Generally, 2.54
Exclusive agency (see Exclusive agency, above)
Exclusive right to sell (see Exclusive right to sell listing, above)
Open listing (see Open listing, above)

LLC. See **Limited Liability Company (LLC)**

Loans. See **Financing**

Local Government
See also **Public Entities**
Annexation of property, 4.91
Building codes. See **Building Codes**
Certificate of Occupancy, 4.105
Environmental clean up orders, cities authorizing, 7.15
Recording documents with county recorder. See **Recordation of Documents**
Residential transfer requirements. See **Residential Purchase and Sale Transactions**
Subdivision, regulating. See **Subdivisions and Subdivision Map Act**
Zoning. See **Zoning**

Loss Adjustments. See **Property Insurance**

Losses. See **Gain or Loss; Risk of Loss**

Mail
Written acceptance of option contract, effect of depositing in mail, 8.20

Malpractice

Attorneys. See **Legal Malpractice**
Real estate agents' errors and omissions insurance. See **Brokers, Dealers, and Real Estate Salespersons**

Management of Hotels. See **Hotels and Motels**

Manufactured Homes
Disclosures in resale of manufactured home, 6.35

Manufacturing Facilities
Dust and dirt contaminants, 7.5

Maps
California coordinate system, 11.18
Circumstantial evidence of legal uncertainty of original map, 11.78
Copies of maps, 11.102
Description of property
Abbreviations, 11.17
Assessor's maps, 11.10, 11.24
Referencing subdivision map, 4.31
North, methods of designating, 11.39
Subdivision Map Act. See **Subdivisions and Subdivision Map Act**

Marital Relationships
Community or separate property. See **Community or Separate Property**
Deeds. See **Deeds**
Disclosure requirements, exemption for transfers between spouses in connection with marital dissolution proceedings, 6.35
Disclosures requirements, exemption for transfers between spouses, 6.35
Homestead property. See **Homestead Property**
Liability insurance for real property transfer, spouse as additional insured, 14.34
Procedural considerations in sale transactions, 4.12, 4.19, App M
Purchase and sale agreement parties. See **Purchase and Sale Agreement**
Registered domestic partners, statute extending rights and responsibilities of marriage to, 6.90-6.91
Spousal waiver, 4.19, App M
Surviving spouse, step-up in basis limited to, 6.91
Title. See **Title**

Marketing Property
See also **Offer To Buy or Sell**
Appraisals. See **Appraisals and Appraisers**
Brokered or nonbrokered sale considerations, 1.105
Financing. See **Financing**
Listing property. See **Listing Agreement; Multiple Listing Services (MLS)**
Negotiated sale or bidding sale, considerations of, 1.106-1.107, 1.111-1.112
Price. See **Price**
Purchaser's use of separate broker, 1.110
Seller's considerations, 1.104
Title marketability. See **Title**
Valuing property. See **Valuation of Property**

Material Loss. See **Risk of Loss**

Measure of Damages. See **Damages**

Mechanics' Liens
Generally, 4.69, 4.78, 4.172
Buyer's protection from claims, 4.69, 4.172
Purchase and sale agreement. See **Purchase and Sale Agreement**
Recording requirement, 4.69, 4.78

Mediation
See also **Alternative Dispute Resolution (ADR); Arbitration**
Pre-litigation and pre-arbitration duty to mediate, 2.153A
Purchase and sale agreement provision, 4.150
Residential purchase and sale agreement, mediation as condition precedent to recovery of attorney fees, 6.19

Memorandum of Option. See **Options**

Metes and Bounds. See **Description of Property**

Military
Emancipated minors serving in military, 4.15
Notice to buyer of former federal or state ordnance locations, 6.44

Property insurance, exclusion for damage caused by military action, 13.87

Mining and Mineral Rights
See also **Oil and Gas**
Reservation of mineral rights, recital in deed, 10.51
Writing unneeded for mineral rights sale, 4.13

Minors
See also **Children**
Capacity to transfer or hold property, 4.7, 4.15
Deed to minor, 10.24, 10.26
Emancipated minors, definition and rights, 4.15
Guardianship. See **Guardianship and Conservatorship**

Misappropriated Funds
See also **Commingling of Funds**
Escrow deposit, 15.22, 15.27
Installment land contract payments, 9.63
Subordination transaction, 9.85

Misrepresentation. See **Fraud and Misrepresentation**

Mistake
Constructive trust, imposition if title obtained through fraud, mistake, or constructive fraud through violation of fiduciary or confidential relationship, 10.19
Covenants of title, effect of mistake invalidating deed, 12.4
Property insurance policy, mistake as grounds for reformation of, 13.25
Purchase and sale agreement rescission grounds, 4.8
Title insurance, negligent errors or misrepresentation, 11.13

Mitigation of Damages. See **Damages**

MLS. See **Multiple Listing Services (MLS)**

Mobilehomes and Mobilehome Parks
Disclosures in resale of mobilehome, 6.35

Modifications. See **Amendments and Modifications**

Mold. See **Hazardous Materials and Toxic Waste**

Monuments
Agreed boundaries doctrine, 11.78
Courses and distances, use of monuments, 11.36
Doctrine of monuments, presumption of intent, 11.31
Metes and bounds, use of monuments, 11.27-11.28
Practical location doctrine, relationship between monuments and deed description, 11.79
Water monuments, 11.81

Mortgage Loan Brokers. See **Brokers, Dealers, and Real Estate Salespersons**

Mortgages and Trust Deeds
See also **Financing**
Accelerating payment on default, 9.47
All inclusive instruments (see Wraparound financing, below)
Ancient mortgages and trust deeds, expiration of, 4.52
Assuming or taking subject to existing trust deed and note
Generally, 4.38, 4.170, 9.48
All-inclusive note and trust deed (see Wraparound financing, below)
Assignment of impound account, 4.133
Credit for existing encumbrances, 9.41
Due-on-sale/encumbrance. See **Due-on-Sale/Encumbrance Clauses**
Government financing transferability, 9.54
Importance of examining preliminary report and promissory note, 4.38
Personal liability of buyer, 4.41-4.42
Computing tax liability when mortgage exceeds basis at time of sale, 9.28-9.29
Construction trust deed, 9.69
Covenant against encumbrances, mortgage as breach of, 12.14
Insurable interest created by, 13.21
Partial reconveyance and release as development progresses. See **Releases**
Pooled mortgage loans, rating and management of, 4.40
Printed forms, 9.42

Property insurance protecting mortgagor's interests. See **Property Insurance**
Real property sales contract, 9.15, 9.17
Reinstatement, 9.47
RESPA. See **Real Estate Settlement Procedures Act (RESPA)**
Seller-financing method, 9.22
Signature requirements, 4.6
Subordination. See **Subordination**
Subrogated rights, 4.42
Witness acknowledgment insufficient to prove execution of mortgage, 15.89
Wraparound financing
Generally, 9.56
Advantages, 9.57
Control over security, 9.59
Drafting considerations, 9.61-9.64
Purchase and sale agreement provision, 9.65
Tax treatment, 9.29, 9.58, 9.60
Usury, 9.6-9.7

Motels. See **Hotels and Motels**

Multiple Listing Services (MLS)
See also **Brokers, Dealers, and Real Estate Salespersons**
Generally, 2.39, 2.74
Disciplinary action against, 2.175
Nonmember access to MLS, 2.41
Residential purchase contract, effect of including or excluding items from MLS on inclusion or exclusion in, 6.8
Subagency, abandonment of automatic offer of, 2.40
Submission of listing to MLS
Cooperation of broker, 2.75
Owner's authorization as requirement for broker submitting listing to MLS, 2.39

Names
Deeds. See **Deeds**
Description of property, name of subdivision, 11.100
Liability insurance policy, named insured under. See **Liability Insurance for Real Property Transfers**

Natural Disasters. See **Disasters**

Natural Hazards, Disclosure of. See **Disclosure**

Navigable Waters
Description of property, 11.81-11.86, 11.110

Negligence
See also **Tort Liability**
Broker's liability for. See **Brokers, Dealers, and Real Estate Salespersons**
Investigate, effect of buyer's duty to, 6.73
Liability insurance. See **Liability Insurance for Real Property Transfers**
Measure of damages
Broker's negligence, 2.159
Negligent performance, 15.22
Recordation of document, recorder's liability for negligence in, 15.87
Title insurance, negligent errors or misrepresentations, 11.13

Negotiation
Letters of intent. See **Letters of Intent**
Marketing property, negotiated versus bidding sale considerations, 1.106-1.107, 1.111-1.112
Option for land acquisition, negotiations concerning purchase price, 8.48
Purchase and sale agreement. See **Purchase and Sale Agreement**
Renegotiating purchase price when undisclosed toxics are found, 7.60
Title policies, negotiating exceptions to, 11.75

Net Proceeds Requirements
Generally, 1.42
Bottom line, 1.43
Client's wants and needs, distinguishing between, 1.44-1.46

Notaries
Acknowledgments, 10.68, 15.89

Notes. See **Promissory Note**

Notice and Notification
Appraisal report, notice of right to receive copy, 9.12
Attorneys. See **Attorneys**
Balloon payment, 9.11
Constructive notice
Acreage, 11.16
Assessor's maps, 11.10
California Coordinate System, description without use of coordinates, 11.22
CC&Rs, 11.7
Conveyance, effect of acknowledgment, 10.1
Defectively acknowledged deeds, 10.6
Defectively acknowledged instrument, 10.70
Defects or exceptions to constructive notice, 15.87
Documentary transfer tax, 10.11
Incomplete, erroneous, or confusing descriptions, 11.91
Inspection of property. See **Inspection of Property**
Nonacknowledging party, no constructive notice of transfer of interest by, 15.89
Option to purchase property, expiration of constructive notice of existence of, 8.18
Overlapping description, 11.89
Person or holding record title changes name, effect of, 10.15, 10.20
Recordation. See **Recordation of Documents**
Recording Act, 12.2
Corporate agent signing conveyance, 4.28
Description of property (see Constructive notice, above)
Disclosures. See **Disclosure**
Easements. See **Easements**
EIR exemption or negative declaration, 4.96
Employee layoff, notice requirements for, 5.18
Encumbrances, effect of grantor's notice on covenant of, 12.7, 12.14
Escrow (see Constructive notice, above)
Federal tax lien, 4.62
Flood insurance requirements, notice concerning, 6.68
Home equity sales contracts, inclusion of statutory notices as prerequisite for enforcement of, 6.108
Inspection of property. See **Inspection of Property**
Instructing tenants to pay rent to buyer, 4.73, App L
Letters of intent as nonbinding, statement in notices, 3.18
Liability insurance, notice of cancellation of, 14.37
Mechanics' liens, 4.69, 4.78
Options. See **Options**
Perform, notice to buyer to (CAR Form NBP), 6.28
Pest control. See **Pests and Pest Control**
Property insurance, notifying insurer of loss covered by, 13.88
Purchase and sale transaction
Generally. See **Purchase and Sale Agreement**
Alternative dispute resolution for sale of real property contracts, format and notice requirements under California law, 6.16
Residential. See **Residential Purchase and Sale Transactions**
Recordation. See **Recordation of Documents**
Removal of tenants, 4.72, 4.74, 4.136
Seller financing, 9.10-9.12, 9.13
Title insurance, notice of advisability of purchasing, 6.66
Toxic substances. See **Hazardous Materials and Toxic Waste**

Nuisance
Contaminated property, owner's right to bring nuisance action based on, 7.20
Disclosure of noisy and disruptive neighbors, 6.31B
Industrial use of property constituting, 6.46

Offer to Buy or Sell
See also **Marketing Property**
Brokers. See **Brokers, Dealers, and Real Estate Salespersons**
Competing offers, agreement not to solicit, 3.11
Multiple offers, 1.108, 1.113
Price issues. See **Price**
Residential transactions, applicability of general principles of contract law governing offer and acceptance, 6.5

Officers of Corporation. See **Corporations**

Off-Records Matters. See **Title**

Offsets

Breach of warranty, offsetting damages by sums buyer owes, 4.107
Remediation costs offset against buyer's note, 7.83

Oil and Gas
See also **Mining and Mineral Rights**
Abandonment of oil and gas interests, 11.80
Leases as *profit a pendre* giving interest in land, 4.71
Petroleum leaks, cause of action, 7.8-7.9
Storage tanks, 7.6

Opening of Escrow. See **Escrow**

Open Listing. See **Listing Agreement**

Options
Generally, 4.4
Advantages and disadvantages for optionor and optionee
Generally, 8.38
Better price, risk optionor will be offered, 8.42
Investigation of property, seller offering prospective purchaser option with ability to conduct, 8.41
Liquidated damages, option as substitute for, 8.39
Tax deferral of option payments, 8.40
Uncertainty of sale, 8.43
Bankruptcy, effect of optionor filing for, 8.28
Broker's commission. See **Brokers, Dealers, and Real Estate Salesperson**
Condemned property subject to option agreement
Generally, 8.31
Portion of condemnation award, optionee receiving, 8.29
Provision in option contract governing, 8.72
Right of first refusal, effect of involuntary condemnation on, 8.58
Consideration for option
Generally, 8.10
Adequacy of consideration, 8.11
Lease, no requirement of consideration for option to purchase in, 8.57
Nonmonetary consideration, 8.13
Other agreements, consideration for options within, 8.12
Provision in option agreement covering, 8.62
Creation of option contract
Generally, 8.8
Essential elements (see Essential elements of option contract, below)
Recording option contracts, 8.18, 8.73
Defined, 8.1, 9.53
Destruction of property, effect on option contract, 8.30-8.31
Disadvantages (see Advantages and disadvantages for optionor and optionee, above)
Due-on-sale provision, option not violation of, 9.53
Enforcement of option, 8.14, 8.33
Essential elements of option contract
Clear and definite terms, requirement for enforceability of option, 8.14
Consideration (see Consideration for option, above)
Rule against perpetuities, effect on term of option, 8.16
Special notices for option agreements, requirement of, 8.17
Statute of fraud, option satisfying requirements of, 8.15
Terms of purchase, 8.9
Exercise of option
Broker receiving commission on, 2.98
Changed terms or added conditions, effect of exercise conditional on, 8.24
Conveyance on exercise of option, 10.46
Method of exercise, option contract prescribing, 8.20
Priority of option on exercise over encumbrance or other interest in property acquired after date of initial option, 8.22
Provision in option agreement for, 8.64
Right of first refusal. See **Right of First Refusal**
Sequential exercise of option, 8.65
Termination of option, failure to exercise option resulting in, 8.32, 8.75
Time period for exercising option, 8.16, 8.21
Waiver of defective exercise of option, 8.23
Extension of option
Lease containing option, effect of extending, 8.57
Provision for successive payments to extend option, 8.63
Financing
Lender's option to purchase interest in property, 8.55
Satisfying lender's conditions to obtain, 8.49
Security instrument, effect of treating option as, 8.54

Form of option agreement
Attorney fees, 8.76
Broker's commission, 8.74
Captions, signatures, 8.80
Condemnation, 8.72
Consideration, 8.62
Covenants and warranties of optionor concerning property, 8.66
Entire agreement, 8.78
Exercise of option (see Exercise of option, above)
Governmental permits, 8.69
Grant of option, 8.60
Introduction, parties, and recitals, 8.59
Investigation of property, 8.68
Memorandum of option, 8.81
Notices, 8.77
Recordation of option, 8.73
Successive payments to extend option term, 8.63
Term of option, 8.61
Time of essence, failure to exercise option, 8.75
Title, condition of, 8.67
Waiver, 8.79
Income tax treatment of option payment
Basis of property, option payments added to, 8.36
Optionor's receipt of payments, treatment of, 8.35
Investigation of property
Developer-optionee, investigation of property by, 8.46
Provision in option contract governing, 8.68
Seller offering prospective purchaser option with ability to investigate property, 8.41
Land acquisition and land use development
Generally, 8.45
Applications for government approval, developer-optionee requiring owner to sign documents as part of, 8.47
Governmental permits, provision in option contract covering, 8.69
Investigation of property by developer-optionee, 8.46
Purchase price, negotiations concerning, 8.48
Lease, option to purchase in. See **Leases**
Memorandum of option
Provision in option contract for, 8.81
Recordation of, 8.18, 8.73
Notice
Provision in option contract governing notices, 8.77
Recording option in county where real estate located resulting in constructive notice to third parties of existence of option agreement, 8.18
Special notices for option agreements, requirement of, 8.17
Price
Negotiations concerning purchase price, 8.48
Risk optionor will be offered better price, 8.42
Remedies, 8.33
Residential option contract, 8.3
Right of first refusal. See **Right of First Refusal**
Risk of loss, 8.71
Tax considerations
Generally, 8.34
Deferral of tax on option payments, 8.40
Income taxes (see Income tax treatment of option payment, above)
Transfer of option right, tax consequences of, 8.37
Termination of option
Generally, 8.32
Exercise of option conditioned on changes in contract terms, termination of option as result of, 8.24
Failure to exercise option resulting in, 8.32, 8.75
Lease termination, effect on option in lease, 8.57
Transfer of option property not resulting in, 8.26
Time. See **Time**
Title insurance and preliminary report
Preliminary report, 8.67
Title insurance for option contract, 8.19
Transferability of options
Assignment of option, 8.25, 8.70
Death of optionee, transferability of option on, 8.27
Tax consequences of, 8.37
Termination of option, transfer of option property not resulting in, 8.26
Two agreements, option contract as
Generally, 8.4

Additional provisions in option contracts for purchase of real property, 8.7
Bilateral contract for purchase and sale, 8.6
Unilateral contract for right of purchase, 8.5
Types of options, 8.2
Uses of options
Generally, 8.44
Exchanges of like-kind property, use of options to facilitate, 8.52
Financing (see Financing, above)
Joint ownership agreements, option clauses in, 8.56
Land acquisition (see Land acquisition and land use development, above)
Lease, option to purchase in. See **Leases**
Multiple parcels, using option contracts to assemble, 8.51
"Put" in favor of seller, 8.53
Right of first offer, 8.58, 8.82
Value, using option contract to tie up property at current market value in expectation of increase in, 8.50
Waiver
Defective exercise of option, waiver of, 8.23
Provision in option contract governing, 8.79

Oral Agreement
See also **Statute of Frauds**
Listing agreement, oral modification of, 2.53
Part performance, 4.13
Purchase and sale agreement
Generally, 4.13
Amendment of purchase and sale agreement by executed oral agreement, 4.162

Orders
Broker's right to administrative hearing on desist and refrain order, 2.174
Contamination abatement or remediation orders, 7.15
Drug lab cleanup order, notice to prospective buyer of, 6.55
Recordation, order of, 9.69

Ownership and Possession
See also **Title**
Adverse possession. See **Adverse Possession**
Agreed boundaries by coterminous owners, 11.78
Agricultural leases, 4.74
Attorney conflict of interest, acquiring ownership or possessory interest adverse to client, 1.7
Change of ownership. See **Change of Ownership**
Contaminated property liability, 7.11-7.14
Contiguous parcels under common ownership subject to merger under Subdivision Map Act, 11.87A
Covenant of seisin, effect of grantor lacking ownership, 12.6
Deed, stating nature of ownership in, 10.29
Description of property. See **Description of Property**
Easements. See **Easements**
Monuments, coterminous owners' duty to maintain, 11.36
Quiet enjoyment and warranty, covenants of, 12.9
Removal of tenants, 4.72, 4.103, 4.136
Risk of loss on buyer when transferring possession of property, 13.8
Water, effect on property ownership rights, 11.81-11.86

Paint. See **Lead-Based Paint**

Parol Evidence
Deeds, proportion of interest stated in deed, 10.30
Description of property
Ambiguity, curing with parol evidence, 11.15
Dominant tenement and easement, 11.65
Statutory rules of construction, 11.98
Sufficiency without parol evidence, 11.14

Partial Performance. See **Performance**

Partial Reconveyance. See **Releases**

Partition
Cotenancy, 4.23
Writing requirement, 4.13

Partnerships

Authority to bind partnership, 4.156
Certificates
General partnership certificate, 4.24
Limited partnership certificate, 4.19, 4.25
Nonforeign status, certificate of, 15.82
Purchase, certificate authorizing, App F
Conveying property
Broker receiving commission if property conveyed to partnership, 2.98
General partnerships, 4.24, 4.156
Limited liability partnerships, 4.26
Limited partnerships, 4.25, 4.156
Prerequisites for partnership property, 4.19
Deeds
Grantor recitals in deed, 10.17, 10.18
Limited partnership, 10.18
Signature of partner, 10.64
Stating nature of ownership in deed, 10.29
General partnerships, 4.24, 4.156
Liability insurance for partnership, individual partners and spouses as additional insureds under, 14.34
Limited liability partnerships, 4.26
Limited partnership interests
Conveyances, 4.25, 4.156
Defective limited partnerships, 4.25
Governing law, 4.25
Grantor recitals in deed, 10.18
Secretary of State filings, 4.19, 4.25
Purchase and sale agreement, 4.24, 4.26, 4.156
Real estate licensee, partner as, 2.4
Recordation
Conveyances by partnership, 10.64
Partnership statement, recordation of, 4.24
Right to contract, 4.24, 4.156
Signature of agent binding on partnership, 4.156
Statute of frauds, 4.13
Tenancy in partnership, holding title as, 6.92
Third parties, effect of partnership statement of authority on, 4.24
Uniform Partnership Act (UPA), generally, 4.24
Yet to be formed entity purchasing property, 4.20

Party Walls, 4.65

Penalties
Brokers. See **Brokers, Dealers, and Real Estate Salespersons**
Criminal penalties. See **Criminal Activity**
Davis-Stirling Act disclosures, penalty for failure to comply with, 6.61
Environmental protection
EPA cleanup order, penalties for failing to comply with, 7.15
Seller's failure to disclose hazardous substances, 7.36
Escrow
Deposit, failure to release, 4.100
Independent escrow companies, monetary fines for violating statutory requirements, 15.4
Withholding requirements, penalties for failure to comply with, 15.79, 15.84
Forfeiture. See **Forfeiture**
Home equity sales contract, penalties for unconscionable acts by equity purchaser, 6.109
Liquidated damages. See **Damages**
Prepayment penalty. See **Prepayment**
Residential Lead-Based Paint Reduction Act, penalties for violation of, 6.51
Smoke detector compliance statement, penalties for failure to deliver, 6.57

Performance
See also **Specific Performance**
Bond securing buyer's obligations, 4.78
Conveyance of title
Effect of performance or nonperformance of condition, 10.2
Performance of sales agreement, 10.45
Escrow conditions. See **Escrow**
Letters of intent, 3.10, 3.14, 3.16, 3.18
Part performance
Consideration, 4.13
Letters of intent, 3.10, 3.14
Oral agreement enforceability, 4.13
Releasing parcels from seller's lien as development progresses. See **Releases**

Severable contract, effect of partial performance by party, 4.164
Specific performance remedy. See **Purchase and Sale Agreement**
Statute extending time for performance of act, inapplicability to acts governed by contractual provisions, 4.152
Time of essence clause, 4.152, 4.178
Title (see Conveyance of title, above)

Permits. See **Licenses and Permits**

Personal Injury
CERCLA, discovery rule for personal injury or property damage under, 7.20
Liability insurance coverage for. See **Liability Insurance for Real Property Transfers**

Personal Property
See also **Intangible Property**
Describing personal property included in sale, 4.33, 4.169, 11.97, 11.118
Exclusion of personal property from sale of real property, 6.8
Liability insurance exclusion eliminating coverage for damage to personal property in care, custody, or control of insured, 14.62
Taxes, lien and proration, 4.61
Transfer as part of real property sale. See **Purchase and Sale Agreement**

Personal Representatives. See **Executors and Administrators**

Pests and Pest Control
Generally, 6.76
Agricultural property contamination by pesticides, 7.3
Allocation of corrections between buyer and seller, 6.76
Common law duty to disclose termite infestation, 6.31A
Inspection report, 6.59
Licensed pest control and home inspection companies performing property inspections, 6.2
Notice
Structural pest control corrective work, notice of completion, 4.79
Work completed and not completed, pest control company completing notice after performing corrective work, 6.76
Structural pest control inspection and repairs, 4.79

Photographs
Description of property, aerial photographs, 11.11
Personal property transferred with real property, photographs of equipment as part of agreement, 11.97

Pollution. See **Hazardous Materials and Toxic Waste**

Possession of Property. See **Ownership and Possession**

Power of Attorney
Deed execution, 10.60
Spousal property transactions, 4.19

Preemption
See also **Federal Preemption**
Condemnation of property for public need preempting private party's preexisting right of first refusal to purchase, 8.29
Timber operations, state timber laws preempting local regulation of, 1.80

Preliminary Report. See **Title Insurance and Preliminary Report**

Premises Liability, 4.78

Prepayment
See also **Acceleration of Payment**
Generally, 9.45
Annual payment limitation, 9.46
Buyer's right to review existing note terms, 4.39, 9.41
First-year payments limitation, 9.45
Penalty
Drafting financing consideration, 4.83, 4.134
Late payment penalty, unenforceability of prepayment penalty acting as, 9.30
Prohibition, 9.52
Seller's restrictions, 9.30-9.31, 9.45
Taking title subject to existing encumbrance, 4.38
Real property sales contract limitation, 9.17
Seller's ability to limit or restrict, 9.30-9.31
Wraparound financing restrictions, 9.62

Pre-Printed Form Agreements. See **Residential Purchase and Sale Transactions**

Presumptions and Inferences
Broker's purchase of client's property, presumptions affecting, 2.132, 10.29
Certificate of limited partnership, presumption created by recording, 4.25
Community property, 4.21, 10.26, 10.29
Deeds
Acceptance, 10.75
Consideration, presumptive evidence of, 10.13
Delivery of deed, rebuttable presumptions, 10.73
Execution of deed by persons listed in recorded partnership statement as presumption of binding conveyance, 10.64
Fee simple title, presumption of, 10.2
Grant deeds, presumption fee simple title passed, 10.2, 10.44
Husband and wife on deed, community property presumption, 10.26
Priority of deeds, presumption on timing, 10.53
Recitals, 10.38
Fee interest. See **Fee Interest**
Fee simple title, presumption affecting passing of, 10.2, 10.44
Government surveys erroneous, presumption official duties properly performed, 11.93
Minor holding property, 4.15
Monument doctrine, presumption of intent, 11.31
Option, presumption affecting assignability of, 8.25
Recorded partnership statement, 4.24
Thread or middle of lake or stream, presumed ownership, 11.83
Title (see Deeds, above)

Price
See also **Marketing Property; Valuation of Property**
Allocation of purchase price, 4.36, 4.182
Appraisals. See **Appraisals and Appraisers**
Balloon payments. See **Balloon Payments**
Broker's advice on. See **Brokers, Dealers, and Real Estate Salespersons**
Contaminated property
Reducing purchase price if buyer shares remediation costs, 7.74
Renegotiating agreement when undisclosed toxics found, 7.60
Covenants of title, price reduced for known encumbrance, 12.18
Deposits (see Purchase and sale agreement deposits, below)
Financing. See **Financing**
Foreign buyer, withholding portion of purchase price under FIRTA, 9.23, 15.80
Imputed interest, 9.36-9.37
Letter of intent, 3.37
Open-ended or contingent sales price, 9.38
Options. See **Options**
Original issue discount (OID), 9.34-9.35, 9.37
Purchase and sale agreement
Adjustment, tenants in possession, 4.72, 4.136
Balance in escrow, 4.37, 4.170
Business operations on property, 4.84, 4.104
Clause regarding purchase price, 4.170
Credits, 4.38
Deposits (see Purchase and sale agreement deposits, below)
Open-ended or contingent, 9.38
Right to buy at lower price, 4.100
Purchase and sale agreement deposits
Generally, 4.37, 4.170
Broker's authority and handling of buyer's deposits, 4.37
Cash downpayment, 9.40
Disbursements of cashier's, certified, or teller's checks, 4.35
Escrow. See **Escrow**
Fixed price and deposit, 4.37
Liquidated damages concerns, 4.141
Mechanics' liens claims, 4.69
Return of deposit, conditional agreement, 4.47, 4.100
Tenants in possession, seller depositing funds to remedy, 4.72, 4.136
Unit price and deposit, 4.35-4.37

Principal and Agent. See **Agents and Agency**

Prisoners
Civil rights, 4.18

Privilege
Environmental audit as privileged information, 1.64

Expert's work, 1.57

Probate Sale
Generally, 1.106
Attorney prohibited from purchasing property at probate sale, 1.7
Brokers' commission, court's approval of, 1.106
Title covenants, effect of probate sale on, 12.22

Procuring Cause of Sale, Broker As. See **Brokers, Dealers, and Real Estate Salespersons**

Professional Responsibility
Attorneys. See **Legal Ethics**
Brokers. See **Brokers, Dealers, and Real Estate Salespersons**

Profits
Property insurance, recovery for lost profits under. See **Property Insurance**
Secret profits. See **Brokers, Dealers, and Real Estate Salespersons**
Writing unneeded for sharing, 4.13

Promissory Note
See also **Financing**
Generally, 9.42
Acceleration on default, 9.47
Annual payments limited, 9.46
Assuming or taking subject to existing note. See **Mortgages and Trust Deeds**
Balloon payments. See **Balloon Payments**
Buyer's right to review existing note securing property, 4.39
Computation of payments, 9.44
Deposit method in purchase and sale transaction, 4.35
First-year payments limited, 9.45
Form of loan documents, 9.42
Prepayment. See **Prepayment**
Remediation costs, offset against buyer's note, 7.83
Security, 4.39, 9.22, 9.43, 9.45-9.47
Seller-financing device, 9.22
Title policy protection, 9.43

Proof
See also **Burden of Proof**
Execution of document, witness acknowledgment insufficient to prove, 15.89
Loss, proof of. See **Property Insurance**

Property Insurance
Generally, 13.1
Additional insured, seller naming buyer as, 13.8
Ancillary coverages for commercial risks
Generally, 13.54
Accounts receivable, 13.68
Business interruption coverage (see Business interruption coverage, below)
Computers (see Computers, below)
Valuable papers and records, separate coverages for, 13.67
Arbitration or appraisal, 13.97
Assignment of, 13.24
Assignment of policy, 13.24
Bad faith
Common law bad faith claim, 13.112
Genuine dispute doctrine, effect of, 13.120
Reverse bad faith by insured, no cause of action for, 13.119
Breach of contract (see Damages, below)
Burden of proof
Business interruption policy, insured's burden of proof under, 13.61
Exclusion barring coverage for loss, insurer's burden of establishing, 13.76
Investigation of claim, insurer's burden to prove prejudice as result of insured's refusal to cooperate with, 13.90
Named risks or named perils policy, insured's burden of proving loss caused by specifically enumerated risks, 13.72
Punitive damages, clear and convincing evidentiary standard requirement for, 13.117-13.117A
Business interruption coverage
Generally, 13.55
Burden of proof, 13.61
Computer operations, optional coverage for interruption of, 13.57
Contingent business interruption coverage and contingent extra expense coverage, availability of, 13.58
Covered causes of loss, 13.56
Described premises, coverage limited to, 13.58

Duty of insured to mitigate damages, 13.62
Exclusions from coverage, 13.55
Extra expense coverage, availability of, 13.63
Period of restoration, beginning date of, 13.60
Pollution Legal Liability policy, coverage for business interruption under, 13.46
Rental value coverage, protection under, 13.64
Total suspension versus partial interruption, 13.59
Cancellation or assumption, 4.106, 4.172
Certificate of insurance not constituting contract between insurer and certificate holder, 13.23
Chinese drywall claims
Generally, 13.137
Direct physical loss, 13.138-13.140
Exclusions, 13.141
Odors caused by release of harmful compounds, 13.139
Safety and habitability issues, 13.140
Claim-related documents, insurer's duty to produce, 13.91
Claims against insurer
Bad faith claims (see Bad faith, above)
Breach of fiduciary duty, no cause of action against insurer for, 13.121
Unfair competition claims, 13.122
Commercial property
Ancillary coverages (see Ancillary coverages for commercial risks, above)
Boiler and machinery coverage, 13.40
Building and personal property, coverage for, 13.38
Business interruption coverage (see Business interruption coverage, above)
Business owners special property, 13.39
Covered causes of loss (see Covered causes of loss, below)
Declarations page for commercial policy stating policy limits for various types of losses, 13.100
Premises burglary, coverage against, 13.43
Replacement cash value, completion of repairs or purchase of substitute property as condition precedent to receiving, 13.103
Robbery and safe burglary coverage, 13.42
Terrorism, insurance against. See **Terrorism**
Theft, disappearance, and dishonesty coverage, 13.41
Computers
Computer fraud, 13.66
Higher limits of coverage for, 13.65
Interruption of computer operations, optional coverage for, 13.57
Loss of data stored electronically not covered under extended coverage for valuable papers, 13.67
Constitutionality of punitive damages
Generally, 13.118
Aggregate disgorgement of profits theory prohibited, 13.118D
Evidence of defendant's net worth required, 13.118E
First guidepost: reprehensibility of defendant's conduct, 13.118A
Second guidepost: disparity between harm suffered by plaintiff and punitives awarded, 13.118B
Third guidepost: court review of difference between punitives awarded and authorized penalties, 13.118C
Continuous or progressive loss
Generally, 13.79
Fortuity, insured's subjective view determining, 13.81
Inception of loss defined, 13.82
Loss in progress doctrine, 13.82
Manifestation rule, liability of insurer at time of appreciable damage for entire progressive loss, 13.80
Contractor working on premises, coverage of, 4.73
Cooperation with insurer's investigation of claim, insured's duty of, 13.90
Copy of insurance policy, insurer providing to insured within 30 days after receipt of request for, 13.88
Covered causes of loss
Generally, 13.70
All risks or all perils policy, 13.71
Mold as, 13.130
Named risks or named perils policy, 13.72
Covered property versus property not covered, 13.69
Criminal acts
Burglary coverage (see Commercial property, above)
Exclusion for, 13.86
Damages
Generally, 13.113
Attorney fees and costs, insured's recovery of, 13.115
Business interruption coverage, insured's duty to mitigate damages, 13.62
Consequential economic losses, insured's recovery of, 13.116
Emotional distress, recovery of damages for, 13.114
Prejudgment interest, recovery of, 13.113
Punitive damages (see Punitive damages, below)
Diminution of value, lack of coverage for, 13.73

Direct physical loss
Generally, 13.73
Chinese drywall claims, 13.138-13.140
Examination under oath, policy requiring insured to submit to, 13.92
Exclusions
Generally, 13.74, 13.86
Burden of proof on insurer to establish applicability of exclusion barring coverage for loss, 13.76
Business interruption coverage, exclusions under, 13.55
Chinese drywall claims, 13.141
Common exclusions, 13.85-13.87
Drafting requirements for, 13.74
Ensuing loss, excluded and not excluded perils combining to cause, 13.84
Exceptions to exclusions, 13.75
Interaction of covered and excluded perils, applicable rule if loss covered by, 13.83
Mold, 13.130
Pollution exclusions under older policies, 13.45, 13.86
Pollution Legal Liability (PLL) policies, exclusions under, 13.48-13.49
Sick-building syndrome, 13.133
Terrorist acts, exclusions related to. See **Terrorism**
Fraud
Coinsured's claim, effect of insured's fraud on, 13.30
Computer fraud, coverage for, 13.66
Reformation of policy, fraud as grounds for, 13.25
Good faith duty between insurer and insured, mutuality of, 13.119
Homeowners policies
Generally, 13.35
California Residential Property Insurance Disclosure form, homeowner's insurer providing insured with, 13.98
Covered causes of loss (see Covered causes of loss, above)
Declarations page for homeowner's policy stating limit of coverage, 13.109
Indemnity
Generally, 13.99
Actual cash value, 13.102
Code-mandated repairs, liability for, 13.107
Coinsurance clauses, 13.110
Deductibles, 13.108
Defined, 13.99
Extended replacement cost, 13.105
Guaranteed replacement cost, 13.104
Homeowners' policies, additional requirements for, 13.109
Inflation guard, 13.106
Inventory, value reporting clauses regarding, 13.111
Policy limits (see Policy limits, below)
Replacement cost value, 13.103, 13.105
Insurable interest as prerequisite for property insurance
Generally, 13.16
Buyer in possession under contract as having insurable interest equal to amount of payments made, 13.18
Existence of insurable interest when policy takes effect and when loss occurs, requirement of, 13.22
Lease, creation of insurable interest under, 13.20
Legal title not required for insurable interest, 13.17-13.21
Mortgage or deed of trust, insurable interest created under, 13.21
Multiple parties having insurable interests, effect of, 13.23
Seller's lack of insurable interest after property sold, 13.19
Landslides and subsidence. See **Landslides and Subsidence**
Lenders and mortgagors, property insurance protecting interests of
Credit bid rule, 13.32
Fraud or arson by insured, effect on coinsured's claim, 13.30
Full credit bid rule, 13.31
Loss payable clause (see Loss payable clause for mortgagee or other lienholder, below)
Secured lenders, insurance on property securing debt, 13.26
Lienholder (see Loss payable clause for mortgagee or other lienholder, below)
Loss payable clause for mortgagee or other lienholder
Generally, 13.27
Simple loss payable clause, 13.28
Standard loss payable clause, 13.29
Loss, risk of. See **Risk of Loss**
Mold, 13.130
Mortgagors (see Lenders and mortgagors, property insurance protecting interests of, above)
Noncommercial property
Generally, 13.33
Condominiums, 13.37
Dwellings, coverage for, 13.36
Fire insurance policy, 13.34

Homeowners policies (see Homeowners policies, above)
Notifying insurance company of loss, 13.88
Occurrence of loss before inception of policy period, coverage for
Generally, 13.77
Continuous loss (see Continuous or progressive loss, above)
Episodic loss, 13.78
Interaction of covered and excluded perils, applicable rule if loss covered by, 13.83
Persons eligible to insure interest in property
Generally, 13.15
Insurable interest (see Insurable interest as prerequisite for property insurance, above)
Policy limits
Declarations page for commercial policy stating policy limits for various types of losses, 13.100
Open versus valued policies, 13.101
Pollution coverage
Exclusions, 13.45, 13.86
Property transfer policies, 13.50
Secured creditor coverage, payment of outstanding loan balance if default occurs and environmental condition exists at location, 13.51
Pollution Legal Liability (PLL) policies, coverage under
Generally, 13.46
Cleanup cost gap coverage, 13.49
Elements of liability defined, 13.47
Exclusions from liability, 13.48-13.49
Profits, loss of
Breach of contract by insurer, insured's recovery of future earnings and profits, 13.116
Business interruption insurance coverage, recovery of lost profits under, 13.55
Progressive loss (see Continuous or progressive loss, above)
Proof of loss
Generally, 13.89
Time limit for filing, 13.88-13.89
Prorating premiums and coverage, 4.133
Punitive damages
Clear and convincing evidentiary standard requirement, 13.117-13.117A
Constitutionality of (see Constitutionality of punitive damages, above)
Corporate entity's liability for punitive damages based on acts or omissions of managing agent, 13.117B
Summary judgment or summary adjudication motions challenging punitive damages claims, 13.117A
Records (see Ancillary coverages for commercial risks, above)
Reformation of policy, 13.25
Risk of loss. See **Risk of Loss**
Sick-building syndrome, 13.133
Standing to assert violation of Unfair Insurance Practices Act, insured's lack of, 13.123
Statute of limitations
Action on the policy, 13.96
Inception of loss determined by reasonable discovery of loss, 13.94
1-year limitations period filing claims, 13.93
Tolling of statute, 13.95
Successive property insurance policies, applicability to continuous damage (see Continuous or progressive loss, above)
Terrorism, coverage against. See **Terrorism**
Time. See **Time**
Transfer of seller's insurance to buyer versus buyer obtaining new insurance, 13.24
Types of property insurance
Ancillary coverages (see Ancillary coverages for commercial risks, above)
Builder's risk policies, 13.44
Commercial property (see Commercial property, above)
Earthquake coverage. See **Earthquakes and Seismic Activity**
Flood insurance. See **Floods**
Noncommercial property (see Noncommercial property, above)
Pollution (see Pollution Legal Liability (PLL) policies, coverage under, above)
Valuation. See **Valuation of Property**

Property Management. See **Hotels and Motels**

Property Taxes. See **Taxes and Tax Assessments**

Proration of Expenses. See **Allocation; Escrow**

Public Entities
See also **Local Government**
Authority to impose remediation orders, 7.15
Dedication of land to public entities and public utilities, 11.77
Easement by prescription prohibited, 11.57
Environmental impact reports, 4.95-4.98

Real Estate Commissioner. See **Real Estate Commissioner**
Secretary of State. See **Secretary of State**
Seller's knowledge of governmental orders or directives, 4.115
Transferability of governmental financing, 9.54

Publicity
Letter of intent as nonbinding, statement in press releases, 3.18, 3.24
Purchase and sale agreement, 4.178

Public Lands
Resurvey, 11.93

Public Policy
CC&Rs, grounds for unenforceability, 4.66
Certainty, public policy prohibiting insurance coverage on, 13.81
Duty to disclose, public policy limitations on, 6.33

Public Utilities. See **Utilities**

Punitive Damages
See also **Damages**
Broker, recovery of punitive damages against, 2.162
Escrow holder's fraud, recovery of punitive damages for, 15.23
Property insurance. See **Property Insurance**

Purchase and Sale Agreement
See also **Residential Purchase and Sale Transactions**
Generally, 4.19
Access to property, 4.90, 4.172
Acreage, 11.16
Agreement of sale, 4.30, 4.169
Alternatives to sale. See **Alternatives to Sale**
Amendments and modifications
Executed oral agreement, modification of written contract by, 4.162
Integration clause, 4.159
Writing requirement, 4.158-4.159, 4.162, 4.178
Annexation of property, 4.91
As-is, 4.49, 4.120, 4.173, 6.9, 7.64, 7.65
Assignment, 4.73, 4.75, 4.155-4.157
Assuming or taking subject to existing trust deed and note. See **Mortgages and Trust Deeds**
Bill of sale, App H
Binding on successors, 4.161, 4.178
Board resolution authorizing purchase, App D
Business operations on property
Buyer's approval of contracts, 4.84, 4.104
Personal property transfers (see Personal property transfer as part of real property sale, below)
Termination of existing contracts, 4.84, 4.104
Warranty against litigation concerning property, 4.116, 4.119
Buyer's use of agents or nominees, 4.156-4.157
Casualty insurance, 4.139
CC&Rs. See **Covenants, Conditions, and Restrictions (CC&Rs)**
Certificates authorizing purchase
Board resolution, App D
Limited liability company, 4.27, App E
Partnership, App F
Choice of law provisions, 4.158, 4.178
Common interest developments. See **Common Interest Developments**
Condemnation provisions, 4.138
Condition of property
Marketability (see Marketable title requirement, below)
Physical (see Physical condition of property and suitability for buyer's intended use, below)
Title insurance. See **Title Insurance and Preliminary Report**
Warranties (see Representations and warranties, below)
Conditions
Generally, 4.3
Access to property, 4.90, 4.172
Approval of onsite investigation and tests, 4.78
Approval of property for buyer's intended operation, 4.85
Approval of reports and surveys in seller's possession, 4.78
Approval of subdivision map, 4.92
Approval of title after reviewing preliminary report, 4.57, 4.60, 4.171
Approval of title subject to preliminary report's stated exceptions, 4.57, 4.171

Business operations on property, buyer's approval of data and contracts, 4.84, 4.104
Buyer's closing conditions, 4.174
CC&Rs. See **Covenants, Conditions, and Restrictions (CC&Rs)**
Financing commitment, 4.3, 4.83
Multiple sellers, 4.128
Obtaining new leases, 4.102
Obtaining required permits, 4.86-4.89
Purpose, 4.121
Recovery of buyer's deposit, 4.100
Relationship to warranty, 4.107
Removal of defects, 4.99, 4.129
Simultaneous exchange, 4.127, 4.165
Structural pest control inspection, 4.79
Subject to another transaction, 4.126, 4.130-4.131
Termination, 4.3, 4.99-4.100, 4.174
Title insurance, 4.111, 4.122
Typical conditions, 4.47, 4.123-4.124, 4.174
Waiver of condition, 4.3, 4.99-4.100, 4.125, 4.128, 4.131, 4.174
Zoning, approval or change, 4.86, 4.113
Confidentiality and publicity, 4.178
Consent issues. See **Consent**
Consideration, 4.6, 4.11, 4.35, 4.86, 4.143
Contaminated property. See **Hazardous Materials and Toxic Waste**
Contractual solutions to common problems
Conditions (see Conditions, above)
Options, 4.4
Warranties (see Representations and warranties, below)
Counterparts, 4.160, 4.178
Covenants, conditions, and restrictions. See **Covenants, Conditions, and Restrictions (CC&Rs)**
Damages
Civil Code §3300, damages under, 4.146
Civil Code §3306, damages under, 4.145
Liquidated damages, 2.119, 4.140-4.143, 4.149
Deeds. See **Deeds**
Defects
Removal of defects, 4.99, 4.129
Seller's representations and warranties in agreement of no cloud on title, buyer's correction or waiver rights, 11.75-11.76
Undisclosed material defects, 4.49, 4.120
Unmarketable title as result of, 4.51
Warranty against material defects, 4.49, 4.120
Definitions or terminology. See **Definitions**
Delivery of documents
Clause regarding, 4.171
Letter instructing tenants to pay rent to buyer, 4.73, App L
Notices, 4.151
Reports and studies, 4.78, 4.171
Warranties and covenants to survive delivery of deed, 4.63, 4.109, 4.111, 12.6
Deposits. See **Escrow; Price**
Description of property. See **Description of Property**
Disclosures
Natural hazard disclosure statement, 4.81, App N
Resale of manufactured home, disclosures in, 6.35
Due diligence. See **Due Diligence**
Easements
Generally, 4.64
Access to property, 4.90, 4.172
Party wall as easement, 4.65
Visible easements, 4.64
Encumbered property, effect of buyer taking
Generally, 9.41
Credits, prepayment penalties, and refinancing costs, 4.38, 9.41
Due-on-sale clause impact, 4.43
Easements (see Easements, above)
Mechanics' liens (see Mechanics' liens, below)
Party walls, 4.65
Personal liability, 4.42
Seller to provide financing, 4.44
Special assessments, 4.63
Tax liens, 4.60-4.62
Enforceability requisites, 4.6, 4.13
Escrow. See **Escrow**
Exchange transaction, tax-deferred treatment, 1.101, 4.127, 4.165, 4.178

Execution and signatures. See **Execution of Documents**
Financing
Generally, 4.3, 4.44, 4.171
Conditions, 4.3, 4.83
Encumbered property (see Encumbered property, effect of buyer taking, above)
Format of agreement, 4.166
Forms and appendices, list of, 4.2
Fraud
Boundary line, misrepresentation of, 4.59
Election of remedies, 4.147
Encroachment impairing buyer's use of asset, seller's liability for misrepresentation when, 4.111-4.112
Rescission grounds, 4.8
Undisclosed material defects, 4.49, 4.120
General provisions, 4.178
Hotel purchase and sale agreement. See **Hotels and Motels**
Inspection of property. See **Inspection of Property**
Installment land contract distinguished, 9.15
Insurance, cancellation or assumption, 4.106, 4.139, 4.172
Intangible property assignment, App J
Integration clause, 4.159
Intent
Letters of intent. See **Letters of Intent**
Third party, intent to make purchase and sale agreement for benefit of, 4.163
Introductory provisions of agreement
Agreement of sale, 4.30, 4.169
Buyer's contingencies, 4.171
Improvements and appurtenances, 4.32, 4.169
Intangible property, 4.34
Legal description of property, 4.31
Personal property, 4.33, 4.169, 11.97, 11.118
Preamble and recitals, 4.29, 4.168
Purchase price, 4.170
Seller's preclosing covenants, 4.172
Title and introductory paragraph, 4.167
Lawful object, 4.6, 4.10
Leases affecting title marketability
Generally, 4.71
Estoppel certificate, 4.73, 4.101, 4.172
New leases issues, 4.102
Purchases free from (see Leases, purchase free from, below)
Purchases subject to (see Leases, purchase subject to, below)
Leases, purchase free from
Removal of tenants, 4.72, 4.103, 4.136
Tenant leases, generally, 4.72, 4.103, 4.136
Leases, purchase subject to
Generally, 4.73
Agricultural leases, 4.74
Ground leases, 4.75
Review of leases, 4.73
Liens
Encumbered property (see Encumbered property, effect of buyer taking, above)
Marketable title requirement (see Marketable title requirement, below)
Mechanics' liens (see Mechanics' liens, below)
Manner of holding title (see Parties' manner of holding title, below)
Marketable title requirement
Generally, 4.50-4.51
Adverse possession, 4.68
Ancient or expired interests, 4.52
Approval of condition of title, 4.57, 4.122, 4.171
CC&Rs. See **Covenants, Conditions, and Restrictions (CC&Rs)**
Defect rendering title unmarketable, 4.51
Easements, 4.64-4.65
Encroachments, 4.58-4.59, 4.67
Existing trust deed and note, examining documents and approving, 4.39
Federal tax liens, 4.62
Lease outstanding (see Leases affecting title marketability, above)
Mechanics' liens (see Mechanics' liens, below)
Party walls, 4.65
Personal property tax liens, 4.61
Real property tax liens, 4.60
Segregating taxes when part of assessed parcel sold, 4.133
Special tax assessments, 4.63

Subdivision Map Act compliance, 4.92, 4.114
Title insurance. See **Title Insurance and Preliminary Report**
Married persons as buyers
Community property presumption, 4.21
Deeds, consent to joint tenancy between one spouse and another person, 10.40
Married persons as sellers, 4.12, 4.19, App M
Mechanics' liens
Generally, 4.69, 4.172
Buyer's protection from claims, 4.69, 4.172
Notice, 4.78
Misrepresentations. See **Fraud and Misrepresentation**
Modifications (see Amendments and modifications, above)
Mortgages and trust deed. See **Mortgages and Trust Deeds**
Mutuality of obligations, 4.30
Negotiation
Generally, 1.114
Assessments, treatment of, 4.63
Attorney's role, 1.116, 1.118
Choice of title company, 4.57
Legal opinions. See **Legal Opinions**
Organizing negotiating team, 1.115
Other counsel, communications with, 1.117
Party wall, 4.65
Warranties, 4.107
Warranties and covenants, 4.109
Notice and notification
Generally, 4.151, 4.172, 4.178
Easements, 4.64
Mechanics' lien issues, 4.78
Natural hazard disclosure statement, 4.81, App N
Options. See **Options**
Oral agreement. See **Oral Agreement**
Parties
Buyer's use of agents or nominees, 4.156-4.157
Capacity to contract, 4.6-4.7, 4.14
Consent, 4.6, 4.8, 4.180
Corporations, 4.28, 4.156
Limited liability companies, 4.27
Manner of holding title (see Parties' manner of holding title, below)
Married persons (see Married persons, above)
Nominees, buyer's use of, 4.156-4.157
Partnerships, 4.24, 4.26, 4.156
Successors, agreement binding on, 4.161, 4.178
Parties' manner of holding title
Entity to be formed, 4.20
Importance of ownership form, 4.21
Married persons as buyers (see Married persons as buyers, above)
Tenancy-in-common agreement, App O
Tenancy-in-common and joint tenancy distinguished, 4.22
Partnership conveyances. See **Partnerships**
Performance
Bond, 4.78
Specific performance (see Specific performance, below)
Time of essence clause, 4.152, 4.178
Personal property transfer as part of real property sale
Description, 4.33, 4.169, 11.97, 11.118
Tax liens, 4.61
Physical condition of property and suitability for buyer's intended use
Generally, 4.77, 4.112, 4.172
Approval of property for buyer's intended operation, 4.85
As-is provisions, 4.49, 4.120, 4.173
Casualty loss, 4.139
Coastal zone property, 4.88
Condemnation provisions, 4.138
Contaminated property. See **Hazardous Materials and Toxic Waste**
Engineering studies and reports, 4.77-4.78
Environmental impact reports, 4.95-4.98
Land surveys, 4.58, 4.67, 4.78
Natural hazard disclosure statement, 4.81, App N
Obtaining required permits, 4.86-4.89
Risk of loss after execution, 4.137, 4.176
Structural pest control inspection, 4.79

Subdivisions. See **Subdivisions**
Zoning issues. See **Zoning**
Possession. See **Ownership and Possession**
Power of attorney, 4.19
Preamble and recitals, 4.29, 4.168
Price. See **Price**
Records and reports
Delivery of reports and studies, 4.78, 4.171
Physical condition of property (see Physical condition of property and suitability for buyer's intended use, above)
Representations and warranties concerning books, records, leases, and contracts, 4.117
Title insurance and report. See **Title Insurance and Preliminary Report**
Remedies
Generally, 4.100, 4.140, 4.144, 4.177
Arbitration, 4.150, 4.177
Attorney fees, 4.142, 4.153, 4.178
Damages (see Damages, above)
Election of remedies, 4.147
Mediation, 4.150
Rescission, mistake as grounds for, 4.8
Specific performance (see Specific performance, below)
Time of essence clause, 4.152, 4.178
Waiver of provision, effect on remedy, 4.143, 4.148, 4.154
Reports (see Records and reports, above)
Representations and warranties
Generally, 4.107, 4.119
Anti-terrorism representations and warranties, 4.119
As-is provisions, 4.49, 4.120, 4.173
Authority, 4.118
Books, records, leases, and contracts, 4.117
Business operations on property (see Business operations on property, above)
Condition of property, 4.49, 4.111, 4.115, 4.120, 4.173
Contracts affecting property, 4.116-4.117
Covenants of title. See **Covenants of Title**
Easements not of record, 4.64
Environmental compliance, warranty and release, 4.80, 4.125
Implied warranties, limits on, 6.30
Knowledge standard, 4.108
Limited warranties, trend towards, 4.110
Material defects, warranty against, 4.49, 4.120
Mechanics' liens, 4.69, 4.172
Merged into deed, 4.109
Negotiations (see Negotiations, above)
No pending governmental action, 4.115
No pending litigation, 4.116, 4.119
Physical condition of property, 4.112
Seller's representations and warranties, 4.173
Subdivision Map Act compliance, 4.92, 4.114
Survive delivery of deed, 4.63, 4.109, 4.111, 12.6
Title warranty, 4.111
Typical buyer's warranties, 4.119
Zoning warranty, 4.86, 4.113
Rescission of, 4.8
Risk of loss of property. See **Risk of Loss**
Severability of agreement, 4.164
Special assessments for public improvements, 4.63
Specific performance
Agreement requisites, 4.6
Execution by buyer's nominee, 4.156-4.157
Failure of condition precedent, 4.100
Liquidated damages availability separate from, 4.142-4.143, 4.149
Unfair release clause's impact on, 9.101
Statute of frauds. See **Statute of Frauds**
Subordination agreement, provision for, 9.78
Surveys. See **Surveys and Surveyors**
Table of exhibits, 4.181
Tax liability, 4.60-4.62, 4.127, 4.133, 4.165, 4.178
Tenancy-in-common agreement, App O
Termination, 4.3, 4.99-4.100, 4.174
Third parties. See **Third Parties**
Time of essence, 4.152, 4.178
Use and development of property (see Physical condition of property and suitability for buyer's intended use, above)
Use of printed forms, 4.5

Waiver
Conditions, waiver of, 4.3, 4.99-4.100, 4.125, 4.128, 4.131, 4.174
Defective title, seller's representations and warranties in agreement of no cloud on title, buyer's correction or waiver rights, 11.75-11.76
Remedies, effect of waiving provisions on, 4.143, 4.148, 4.154
Warranties (see Representations and warranties, above)
Williamson Act, land subject to, 4.93
Writing requirement
Generally, 4.6, 4.12
Amendments and modifications, 4.158-4.159, 4.162, 4.178
Certainty of property description, 4.9
Notices, 4.151
Statute of frauds, 4.13
Zoning issues. See **Zoning**

Purchase Price. See **Price**

Questionnaires. See **Charts, Checklists, Questionnaires, and Tables**

Questions of Law and Fact
Agency's existence as question of fact, 2.28
Brokers
Performance with diligence as question of fact, 2.148
Procuring cause of sale as question of fact, 2.99
Discoverability of defects during inspection of property, 4.49
Grantor's intent to transfer title as question of fact, 10.71
Obvious and patent conditions as question of fact, 6.72
Project having significant impact on environment, 4.95
Seller's knowledge of undisclosed fact as question of fact, 6.30
Upper landowner changing natural drainage system, reasonableness, 4.77

Quiet Enjoyment
Breach of covenant of quiet enjoyment, 12.9, 12.15

Quiet Title
Generally, 11.112
Ambiguity, description supplemented in later deeds adding, 11.96
Boundaries on tidal and submerged lands, 11.82
Breach of condition, action for quiet title, 10.50
Erroneous survey, 11.93
Failure to close metes and bounds description, 11.90
Incomplete, erroneous, or confusing description in deed, 11.91
Overlapping descriptions, 11.89

Quitclaim Deeds. See **Deeds**

Racial Discrimination. See **Discrimination in Housing Market**

Railroads
Description of property, railroad rights-of-way, 11.31
Rights-of-way, construing easements, 11.31, 11.71

Ready, Willing, and Able Buyer. See **Brokers, Dealers, and Real Estate Salespersons**

Real Estate Commissioner
Brokers and salespersons, disciplinary proceedings against, 2.171-2.174
Real property sales contracts in subdivision offerings, regulations, 9.17

Real Estate Fund. See **Brokers, Dealers, and Real Estate Salespersons**

Real Estate Settlement Procedures Act (RESPA)
Generally, 15.95
Kickbacks, referral fees, and other unearned fees prohibited under, 2.135
Settlement statement, 15.95, App Y

Receivers and Receivership
Lender's remediation of contaminated property, 7.94

Reconveyance. See **Releases**

Recordation of Documents
Adverse possession, reducing to record, 4.68
Affidavit of joint tenant's death, 4.19
Agent of grantee or mortgagee, recorder as, 15.92
CC&Rs, 4.66, 11.7
Certified documents, recording of, 15.90
Constructive notice
Conveyance, constructive notice provided by recordation of, 15.86
Real property located in multiple counties, recording document in one county giving constructive notice in county of recordation, 15.90
Requirements for constructive notice, 15.92
Covenants, recordation of. See **Covenants**
Deeds
Adequate funds to pay for real property, recordation of deed after escrow holder receives, 15.1
Construction trust deed, 9.69
Phrases required for recording, 10.8-10.10
Taxes. See **Taxes and Tax Assessments**
Description of property
Railroad rights-of-way, reference to recorded map, 11.31
Reference to other recorded instruments, 11.25
Subdivision or parcel maps, 11.24
Sufficient identification of property without coordinates, 11.22
Escrow
Generally, 15.85
Accommodation recording, 15.24
Adequate funds to pay for real property, recordation of deed after escrow holder receives, 15.1
Effect of recording conveyance, 15.86
Priority for recording documents, 15.47
Procedures (see Procedures for recording escrow documents, below)
Federal tax lien, 4.62
Home inspection report, 6.77
Indexing by recorder, 15.91
Lease with option to purchase, recordation of, 9.18, 10.46
Limited liability company documents, 4.27
Limited partnership certificate, 4.25
Mechanics' lien issues, 4.69, 4.78
Negligence in recording document, recorder's liability for damages, 15.87
Notice
Completion of work, 4.105
Constructive notice (see Constructive notice, above)
Lis pendens, notice of, 4.116
Off-record easements. See **Easements**
Option agreement, 8.18, 8.73
Overview of Recording Act, 12.2
Partnerships. See **Partnerships**
Postclosing follow-up by attorney, receipt and review of recorded documents, 1.143
Power of attorney, 4.19
Procedures for recording escrow documents
Acknowledgment of signature, requirement that document contain, 15.89
Form of instrument, 15.88
Place of recording, 15.90
Recorder's procedure, 15.91
Timing of recording, 15.92
Property insurance, ancillary coverage for valuable papers and records, 13.67
Releases, 9.100
Retroactive recordation as remedy for recorder's improper delay, 15.92
Special recording, 15.42
Subdivision map, 4.92, 11.24
Subordination documents, 9.69, 9.82
Superiority of tax liens over earlier recorded private liens, 4.60
Unlocatable documents, effect of improper indexing, 12.2
Unrecorded interests, 12.3
Wild document, 15.91

Records and Reports
Accounts and accounting. See **Accounts and Accounting**
Agricultural lands held by foreign investors, reporting requirements, 1.89
Appraisal report, right to receive copy, 9.12
Client funds, attorney's maintenance and retention of records on, 1.12
Destroyed land records, remedy in rem to establish record title in event of, 11.117
Electronic record defined, 2.47, 4.12
Engineer's reports, 4.77-4.78

Environmental audits. See **Hazardous Materials and Toxic Waste**
Environmental impact reports, 4.95-4.98
Escrow
Preliminary change in ownership report (PCOR), 15.99, App BB
Unclaimed funds, escrow holder filing annual report with State about, 15.25
Foreign investments, reporting requirements, 1.89
Legal opinions. See **Legal Opinions**
Liability insurance policy, reporting claims under. See **Liability Insurance for Real Property Transfers**
Preliminary report. See **Title Insurance and Preliminary Report**
Property insurance, value reporting clauses regarding inventory, 13.111
Purchase and sale agreement. See **Purchase and Sale Agreement**
Structural pest control inspection, 4.79

Recovery Account. See **Brokers, Dealers, and Real Estate Salespersons**

Redemption
Deed in lieu of foreclosure, effect on redemption right, 10.41

Reformation
Erroneous survey, 11.93
Failure to close metes and bounds descriptions, 11.90
Incomplete, erroneous, or confusing description in deed, 11.91
Property insurance policy, reformation of, 13.25

Reimbursement
Liability insurer seeking reimbursement of defense costs for claims not potentially covered, 14.56
Recovery Account of Real Estate Fund, broker or salesperson reimbursing after payment of claim, 2.170

Reinstatement
Deed in lieu of foreclosure, effect on reinstatement right, 10.41

Relatives. See **Family Members**

Releases
See also **Indemnity**
"As-is" clauses. See **As-is Clause**
Buyer's assumption of existing debt, 4.41, 9.48
Contaminated property. See **Hazardous Materials and Toxic Waste**
Easement, release of, 11.108
Environmental, 4.80, 4.125
Escrow deposits, 4.37, 4.100, 4.170
Federal estate tax lien, 4.62
Indemnity compared, 7.66
Partial reconveyance as buyer develops parcels
Generally, 9.22, 9.39, 9.100
Certainty and fairness requirement, 9.101-9.102
Condemnation award release, 9.110
Impact on damages, 9.102
Impact on specific performance, 9.101
Partial release (lots not determined) with adjustment of release price, 9.107
Partial release (lots not determined) with buyer's discretion limited, 9.106
Partial release of determined lots, 9.105
Subdivision requirements, 9.103-9.104
Substituted security for releases, 9.109
Unencumbered conveyance at close of escrow, 9.108
Recital in deed, release of exception or reservation, 10.44
Reconveyance
Breach of condition, action to compel reconveyance, 10.50
Partial (see Partial reconveyance as buyer develops parcels, above)
Partner not authorized to convey property, 10.64

Reliance. See **Detrimental Reliance**

Remediation of Contaminants. See **Hazardous Materials and Toxic Waste**

Remedies
Alternative dispute resolution. See **Alternative Dispute Resolution (ADR)**
Arbitration. See **Arbitration**
Broker misconduct. See **Brokers, Dealers, and Real Estate Salespersons**
Covenants of title, remedies for breach. See **Covenants of Title**
Damages. See **Damages**
Declaratory relief. See **Declaratory Relief**

Equitable relief. See **Equitable Relief**
Hazardous substances on residential property. See **Hazardous Materials and Toxic Waste**
Indemnity. See **Indemnity**
Injunctions. See **Injunctions**
Lease-option as hidden security device, 9.21
Mediation. See **Mediation**
Option contract to purchase real property, 8.33
Purchase and sale agreement breach. See **Purchase and Sale Agreement**
Quiet title. See **Quiet Title**
Reformation. See **Reformation**
Rescission. See **Rescission of Transaction**
Retroactive recordation of document as remedy for recorder's improper delay, 15.92
Subdivision Map Act noncompliance, 4.92
Tenants remain after closing, 4.72, 4.73, 4.103, 4.136

Rents
See also **Income-Producing Property; Investments; Leases**
Business interruption policy, rental value coverage as part of, 13.64
Escrow
Seller's separate escrow instructions, proration of rents, 4.133
Transfer of post-closing rents to buyer, instructions to escrow holder on, 15.46
Instructing tenants to pay rent to buyer, 4.73, App L
Letter to tenant on transfer of lease under sale of property, App L
Proration in purchase and sale transaction, 4.72, 4.133, 4.175
Rent control concerns, 4.72
Taxation of, 9.21
Tenant's estoppel certificate, 4.73, 4.101, 12.7, App K

Repairs
Generally. See **Construction, Improvements, and Repairs**
Remediation. See **Hazardous Materials and Toxic Waste**

Reports. See **Records and Reports**

Representations and Warranties
See also **Covenants of Title**
Breach of warranty, offsetting damages by sums buyer owes, 4.107
Defective title, 4.111, 11.75-11.76
Hazardous materials. See **Hazardous Materials and Toxic Waste**
Hotel purchase and sale agreement, seller's representations and warranties, 5.16, 5.17
Implied warranty of merchantability and covenant of title distinguished, 12.1
Knowledge standard, 4.108
Letter of intent, 3.42
Liability insurance. See **Liability Insurance for Real Property Transfers**
Option contract for purchase of real property, warranties of optionor, 8.66
Purchase and sale agreement. See **Purchase and Sale Agreement**
Structuring transaction, warranty considerations, 1.100
Surviving delivery of deed, 4.63, 4.109, 4.111
Warranty deeds, 4.109, 10.5, 12.9

Resales
Brokers. See **Brokers, Dealers, and Real Estate Salespersons**
Manufactured home, disclosures in resale of, 6.35

Rescission of Transaction
Common law duty of disclosure, rescission as remedy for breach of, 6.30
Purchase and sale agreement, 4.8

Residence
Definition of principal residence, 15.76
Homestead. See **Homestead Property**
Purchase and sale. See **Residential Purchase and Sale Transactions**

Residential Purchase and Sale Transactions
See also **Exchange of Property; Purchase and Sale Agreement**
Generally, 6.1
Alternative dispute resolution (ADR)
Generally, 6.15
Exclusions from arbitration under California law, 6.17
Federal Arbitration Act, preemption of state law under, 6.15, 6.18-6.18A
Format and notice requirements under California law, 6.16
Arranger of credit defined, 9.10

Attorney's role in residential transactions, 6.2
Bank-owned (REO) sales
Generally, 6.110
REO advisory (CAR Form REO), 6.111
Broker's commission, conditions created by purchase agreement and receipt for deposit, 2.113
California Association of Realtors (CAR) residential property forms
Generally, 6.3
California Residential purchase agreement and joint escrow introductions (CAR Form RPA-CA), 6.24
Notice to buyer to perform (CAR Form NBP), 6.28
Purchase and agreement addendum (CAR Form PAA), 6.26
Short sale addendum (CAR Form SSA), 6.28A, 6.106D
Statewide buyer and seller advisory (CAR Form SBSA), 6.27
Common interest developments. See **Common Interest Developments**
Conditioned on sale of buyer's residence, 4.131
Contingencies
Generally, 6.20
Conditions precedent, 6.21
Removal of, 6.22
Damages (see Liquidated damages, below)
Delivery of documents. See **Delivery of Documents**
Description of property in standard form agreement
Fixtures and personal property, 6.8
Real property, 6.7
Disclosure obligations
Generally. See **Disclosure**
Agency relationship. See **Brokers, Dealers, and Real Estate Salespersons**
Discrimination restrictions. See **Discrimination in Housing Market**
Due diligence. See **Due Diligence**
Escrow holder's functions in residential transactions, 15.17
Financing. See **Financing**
Home equity sales contracts
Generally, 6.107
Enforceability of, 6.108
Prohibited conduct during 5-day cancellation period, 6.109
Remedies for unconscionable conduct by equity purchaser, 6.109
Inspections. See **Inspection of Property**
Liquidated damages
Forfeiture of buyer's deposit on default, 6.13
Formal requirements for liquidated damages provision, 6.11
New condominiums, special rules governing liquidated damages provision in initial sale of, 6.14
Owner-occupied one-to-four units, 6.10-6.13
Reasonableness requirement, 6.12
Notice
Alternative dispute resolution, format and notice requirements under California law, 6.16
Perform, notice to buyer to (CAR Form NBP), 6.28
Option for, 8.3
Possession. See **Ownership and Possession**
Prepayments and prepayment penalties, 9.30-9.31
Pre-printed form agreements (see Standard form agreements, below)
Purchase price. See **Price**
Rent control concerns, 4.72
Risk of loss. See **Risk of Loss**
Standard form agreements
Generally, 6.3
Alternative dispute resolution (see Alternative dispute resolution (ADR), above)
"As-is" clauses, effect of, 6.9
Attorney fees, 6.19
Contingencies (see Contingencies, above)
Description of property (see Description of property in standard form agreement, above)
Estimate of closing costs, escrow agent providing to buyer and seller, 6.23
Handwritten terms superseding printed pre-printed form provisions, 6.4-6.5
Liquidated damages (see Liquidated damages, above)
Offer, acceptance, and counteroffer, general principles of contract law governing, 6.5
Statutory rules of contract interpretation, applicability to pre-printed form agreements, 6.4
Transaction costs, allocation or proration between buyer and seller, 6.23
Tax considerations
Generally, 6.93
Capital gains tax on sale of principal residence, 6.97
Property tax, 6.96
State and federal withholding taxes, 6.94
Transfer tax, 6.95
Title insurance and report. See **Title Insurance and Preliminary Report**

Title. See **Title**

Residential Stock Cooperatives
See also **Common Interest Developments**
Coastal zone property, 4.88

Resorts. See **Hotels and Motels**

Resource Conservation and Recovery Act of 1976 (RCRA), 7.8

RESPA. See **Real Estate Settlement Procedures Act (RESPA)**

Retroactivity
Exemption from usury limitations for loan secured by real property and made or arranged by real estate broker, retroactive effect of, 2.9
Recorder's improper delay in recording document, retroactive recordation of document as remedy for, 15.92

Right of Entry
Generally. See **Access to Property**
Easements. See **Easements**

Right of First Refusal
Generally, 8.58
Condemnation of property for public need preempting private party's preexisting right of first refusal to purchase, 8.29
Options
Consideration for option contained within, 8.12
Provision in option contract for right of first refusal, 8.83

Rights-of-Way
Description of, 11.25
Easements. See **Easements**
Streets. See **Streets, Roads, and Highways**

Risk (Generally)
Client's risk tolerance, postsale contingencies
Generally, 1.50
Condition of property, 1.52
Miscellaneous postsale problems, 1.53
Seller financing, 1.51
Client's risk tolerance, presale contingencies, 1.47
Description of property, 11.2
Option contract, risk optionor will be offered better price, 8.42
Purchaser's presale risk tolerance, 1.49
Seller's presale risk tolerance, 1.48

Risk of Loss
See also **Gain or Loss**
After execution of purchase and sale agreement, 4.137, 4.176
Assumption of risk
Agreement to insure by buyer, 13.11-13.12
Buyer's assumption of risk, 13.9
Option contract, provision governing risk of loss, 8.71
Possession by buyer before transfer of title, 13.8
Seller naming buyer as additional insured in seller's policy, 13.8
Seller's assumption of risk, 13.10
Contingent or unknown event as requirement for insuring against risk of loss, 13.81
Damage or destruction before completion of sale
Generally, 13.2
Assumption of risk (see Assumption of risk, above)
Material loss (see Material loss, below)
Nonmaterial loss (see Nonmaterial loss, below)
Uniform Vendor and Purchaser Risk Act, 4.137-4.138, 13.3, 13.6, 13.13
Material loss
Absence of agreement, allocation of loss in, 13.4
Breach by buyer, effect of material loss after, 13.14
Defined, 13.5
Nonmaterial loss
Absence of agreement, enforcement of contract in, 13.6
Form, risk of nonmaterial loss, 13.7

Roads. See **Streets, Roads, and Highways**

Rule Against Perpetuities
Option, effect of rule on exercising, 8.16

Rules of Professional Conduct for Attorneys. See **Legal Ethics**

Safe Deposit Boxes
Hotel purchase and sale agreement, provision affecting contents of safe deposit boxes, 5.28

Safety. See **Health and Safety Standards**

Salaries and Compensation
Brokers. See **Brokers, Dealers, and Real Estate Salespersons**
Business interruption insurance coverage, recovery of lost earnings under, 13.55
Secret profits or commission. See **Brokers, Dealers, and Real Estate Salespersons**

Salespersons. See **Brokers, Dealers, and Real Estate Salespersons**

Sales Tax
Hotel's personal property, sales tax on sale of, 5.29

Sanctions. See **Penalties**

Secretary of State
Corporation filings, 4.28
Limited liability company filings, 4.27
Limited liability partnership filing, 4.26
Limited partnership filing, 4.19, 4.25

Secret Profits or Commission. See **Brokers, Dealers, and Real Estate Salespersons**

Secured Transactions
Generally, 9.43
Foreclosure. See **Foreclosure**
Hazardous substances concerns. See **Hazardous Materials and Toxic Waste**
Installment land contract, 9.14, 9.16
Lease-option as hidden security device, 9.19-9.21
Mortgages and trust deeds. See **Mortgages and Trust Deeds**
Partial reconveyance and release as development progresses. See **Releases**
Performance bond securing buyer's obligations, 4.78
Subordination. See **Subordination**

Security
See also **Financing**
Attorney conflict of interest, acquiring security interest adverse to client, 1.7
Deed in lieu of foreclosure, 10.41
Option, effect of treating as security interest, 8.54
Promissory note, 4.39, 9.22, 9.43, 9.45-9.47
Witness acknowledgment insufficient to prove execution of security agreement, 15.89

Seisin
Defect in title and covenant of seisin and good title, 12.6, 12.13

Seismic Activity. See **Earthquakes and Seismic Activity**

Self-Dealing by Broker. See **Brokers, Dealers, and Real Estate Salespersons**

Senior Citizens
Federal and state antidiscrimination provisions, exemption for senior citizen housing, 6.103
Residential facility for elderly, inapplicability of recorded covenants permitting only residential use of property to, 6.104

Separate Property. See **Community or Separate Property**

Setoffs. See **Offsets**

Settlement Under RESPA. See **Real Estate Settlement Procedures Act (RESPA)**

Sexual Conduct
Harassment, escrow holder's liability for, 15.22

Sexual Offenses
Disclosure of information about data base of registered sex offenders (Megan's Law), 6.56

Short Sales
Generally, 6.106C
Broker's duty regarding, 2.147A
Lender's evaluation and requirements, 6.106E
Short sale addendum (CAR Form SSA), 6.28A, 6.106D
Tax considerations, 6.106F

Sick-Building Syndrome. See **Property Insurance**

Signatures. See **Execution of Documents**

Slander of Title
Escrow holder's liability for, 15.22

Smoke Detectors
Disclosure requirements concerning, 6.57

Social Security
Real estate salesperson, withholding social security from compensation of, 2.19

Soil
Contamination. See **Hazardous Materials and Toxic Waste**
Testing of, 4.77

Specific Performance
See also **Performance**
Description of property, sufficiency to support specific performance, 11.15
Letters of intent, 3.13-3.14
Purchase and sale agreement. See **Purchase and Sale Agreement**
Uniform Vendor and Purchaser Risk Act, buyer's lack of entitlement to specific performance with reduction in price in event of damage to property, 13.3

Spouses. See **Marital Relationships**

Standing
Unfair Insurance Practices Act, insured's lack of standing to assert violation of, 13.123

State Department of Toxic Substances Control
Hazardous wastes list, 7.9

Statute of Frauds
See also **Oral Agreement**
Amendments to agreement, 4.158-4.159, 4.178
Brokers
Agency relationship with seller not subject to statute of frauds, 2.125
Commission (see Commission for brokers, below)
Contents of required writing, 2.44-2.47
Employment of broker, writing establishing, 2.45
Exceptions to statute of frauds, 2.52
Execution of writing, 2.47
Identification of property in writing, requirement of, 2.46
Oral modification of listing agreement, 2.53
Theories of recovery in absence of writing (see Theories of recovery in absence of writing, below)
Commission for brokers
Listing agreement, statute of frauds prohibiting recovery of commission if broker procures buyer after expiration of, 2.115
Writing as prerequisite for recovery of, 2.27, 2.43, 2.48, 2.95
Description of property, 4.9, 11.14-11.15
Estoppel theory, 4.13
Leases, 10.1
Letters of intent, 3.25-3.26
Memorandum of agreement satisfying statute of frauds, 2.95
Noncompliance consequences, 4.13
Option contract for purchase of real property, effect of statute of frauds on, 8.15
Purchase and sale agreement
Generally, 4.13
Description of property, 4.9
Theories of recovery in absence of writing
Estoppel theory, broker's inability to recover commission based on, 2.51
Misrepresentation by principal, broker's recovery for fraud based on, 2.50
Quasi-contract theory, broker's inability to recovery from seller on, 2.49

Statutes of Limitations
See also **Laches; Time**
Breach of contract action, 15.22
Breach of duty to disclose, statute of limitations for, 2.183
Brokers
Disciplinary proceedings, statute of limitations for, 2.173
Third party actions against brokers, statute of limitations for, 2.178
CEQA actions, 4.98
Contractual indemnity action, statute of limitations for, 2.183
Covenants of title. See **Covenants of Title**
Defectively acknowledged instrument, constructive notice, 10.70
Property insurance. See **Property Insurance**
Quiet title action, statute of limitations accruing on presentation of adverse claim to title, 11.112
Reclaiming land bank carried away by water, 11.86
Subdivision Map Act violation, 11.24
Trespass action for injuries to real property, 7.20

Stay of Proceedings
Bankruptcy, automatic stay in, 9.47

Stock Cooperatives. See **Residential Stock Cooperatives**

Storage Tanks
Leakage, 7.6, 7.9
Underground storage tanks, disclosure requirements concerning, 6.53

Streets, Roads, and Highways
See also **Transportation**
Abandoned roads reverting to fee owner, 4.58
Access to property. See **Access to Property**
Description of property
Easements. See **Easements**
Filing of map as declaration of right to use streets and passageways, 11.24
Inspection disclosing street rights-of-way, 11.11
Metes and bounds using streets and public rights-of-way, 11.30
Design and improvements, 4.92
Easements. See **Easements**
Implied dedication, 11.77

Strict Liability
CERCLA, strict liability under, 7.10
Surface waters, 4.77

Structure of Transaction, Reviewing With Client. See **Attorney-Client Relationship**

Subdivisions and Subdivision Map Act
See also **Developers**
Approval of map, 4.92
Basic considerations, 1.83
CC&Rs. See **Covenants, Conditions, and Restrictions (CC&Rs)**
Contiguous parcels under common ownership subject to merger under Subdivision Map Act, 11.87A
Definitions
Design and improvements, 4.92
Subdivision, 1.83, 4.92
Description of, 4.31, 11.4, 11.8, 11.24, 11.100
Dividing property in violation of Subdivision Map Act, effect on marketability of title, 4.55
Dominant tenement, effect of subdividing on easement, 11.65
Endorsement, 4.92, 4.114
Need for map and related approvals, 4.92
Presumption affecting conveyance subject to restrictions on use imposed as part of common interest developments, 10.2
Purchaser due diligence considerations, 1.79
Real property sales contracts in subdivision offerings, 9.17
Recordation of map, 4.92, 11.24
Releasing buyer's parcels from seller's lien, subdivision requirements, 9.103-9.104
Seller's alternative, subdividing property, 1.31
Streets and alleys reflected on subdivision map, right to use, 11.46
Transfer voidable, violation of Act, 11.24
Vesting tentative map, effect of, 1.84

Subordination
Generally, 9.22, 9.66, 9.74
Agreement

Cautionary language (see Cautionary language, below)
De facto, 9.88
Executed (see Executed subordination agreement, below)
Executory (see Executory subordination agreement, below)
Antideficiency rules, effect on, 9.9, 9.95-9.99
Cautionary language
Generally, 9.89
Agreement permits proceeds to be used for other than improvement purposes, 9.93
Automatic subordination, 9.90
Right to waive, 9.94
Security instrument permitting proceeds to be used for other than improvement purposes, 9.91
Security interest becoming junior, 9.92
Competing factors, 9.67
De facto subordination agreement, 9.88
Executed subordination agreement
Generally, 9.83
Automatic subordination agreement, 9.86, 9.87
Discrepancy between agreement and loan, 9.84
Misapplication of funds, 9.85
Executory subordination agreement
Generally, 9.73-9.74
Addendum, 9.79, 9.80-9.82
Enforceability requirements of certainty and reasonableness, 9.75
Optional terms, 9.77
Purchase and sale agreement provision, 9.78
Required terms, 9.76
Lien, waiver of subordinated, 9.94, 9.96-9.97
Methods of providing first lien
Generally, 9.68
Automatic and by agreement, 9.70
Order of recordation, 9.69
Recordation of documents, 9.69, 9.82
Seller's benefits and protections, 9.72
Seller's risks, 9.71-9.72
Spangler case, 9.95-9.98
Take-out or permanent financing, subordinating to, 9.76, 9.81-9.82

Suretyship. See **Bonds and Undertakings**

Surveys and Surveyors
See also **Engineers**
Generally, 4.58-4.59
Approval by buyer, 4.78
Constructive notice, survey not providing, 15.87
Costs responsibility, 4.78, 4.134
Description of property
ALTA policy with survey endorsement, 11.75
Alternative surveying and mapping systems, 11.23
Base and meridian landmarks, 11.18
California Coordinate System, 11.22
Certainty requirement, 11.14
Confirming by survey, 11.2, 11.12
Curves, 11.32
Easements, 11.6
Failure to close metes and bounds description, 11.90
Fraudulent or erroneous surveys, resurveys, 11.93
Government surveys (see Government surveys, below)
Incomplete, erroneous, or confusing description, valid description from surveyor, 11.91
Monuments, 11.27-11.28
Referring client to surveyor, 11.3
Rights-of-way, 11.25
Surveyors role, 11.8, 11.11
Zoning and subdivision considerations, 11.4
Encroachments, 4.67
Environmental audits. See **Hazardous Materials and Toxic Waste**
Government surveys
Description by reference to rectangular survey map, 11.101
Quarters, 11.21
Range and township, 11.19
Referring to in description, 11.17
Section, 11.20
Party wall, 4.65

Surviving Spouse
Step-up in basis limited to, 6.91

Tables. See **Charts, Checklists, Questionnaires, and Tables**

Taxes and Tax Assessments
Agricultural property. See **Agricultural Property**
Attorney's advice on tax issues, 1.20
Basis of property. See **Basis**
Brokers. See **Brokers, Dealers, and Real Estate Salespersons**
Capital gains tax. See **Gain or Loss**
Change of ownership. See **Change of Ownership**
Dealers, 9.32
Deferred payment to seller
Buyer's financing needs relationship, 9.39
Installment method (see Installment method of reporting gain, below)
Open-ended or contingent sales price, 9.38
Promissory note secured by mortgage or trust deed, 9.22
Seller's conflicting desires, 9.39
Disclosure requirements. See **Disclosure**
Easement by prescription, tax payment as element of, 11.57, 11.77
Escrow. See **Escrow**
Exchange transactions, 4.127, 4.165, 4.178
Financial objectives, tax consequences of transaction, 1.54
FIRPTA. See **Foreign Investment in Real Property Tax Act (FIRPTA)**
Foreign person as property seller, federal withholding requirements, 1.89
Gain or loss. See **Gain or Loss**
Hotel purchase and sale agreement, provision for proration of taxes, 5.26
Imputed interest rules, 9.36-9.37
Installment method of reporting gain
Generally, 9.24-9.25
Computation examples, 9.26-9.28
Dealers, 9.32
Disposition of obligations, 9.33
Imputed interest, 9.34, 9.36-9.37
Lease-option payments, 9.20-9.21
Original issue discount, 9.34-9.35
Prepayment limitations, 9.30-9.31
Wraparound financing, 9.29, 9.58, 9.60
Joint tenancy termination as change of ownership for property tax, 4.22
Legal fees, taxability of, 1.20
Liens
Federal taxes, 4.62
Personal property taxes, 4.61
Real property taxes, 4.60
Special assessments, 4.63
Like-kind exchanges, 1.101, 4.127, 4.165
Mello-Roos Community Facilities Act or Improvement Bond Act of 1915, seller obtaining disclosure notice regarding special tax or assessment under, 6.42
Option contract for purchase of real property, tax considerations affecting. See **Options**
Original issue discount (OID) obligations, 9.34-9.35
Personal property tax, 4.61
Proration of taxes, 4.133
Public improvements, 4.63
Purchase and sale agreement, tax liability under, 4.60-4.62, 4.127, 4.133, 4.165, 4.178
Purchase price, allocation for income tax purposes, 4.36
Real property transfers
Disaster, transferring base-year value of damaged property to comparable replacement property, 6.96
New base-year value for assessing property taxes, 1.96
Proration and reassessment before closing, 4.133
Proration of, 4.60, 15.44
Reappraisal triggering events, App A
Residential purchase and sale transaction, effect on property tax, 6.96
Segregation when part of assessed parcel sold, 4.133
Supplemental property tax bill, notifying prospective buyer of, 6.43
Supplemental tax bills after closing, 4.133
Tax-deferred exchange, 1.101, 4.127, 4.165, 4.178
Tax lien, 4.60
Recapture income, 9.27
Recording deeds

Documentary transfer tax, 10.11, 10.12
Tax statements required, 10.10
Rent payments, 9.21
Residential purchase. See **Residential Purchase and Sale Transactions**
Sales tax on sale of hotel's personal property, 5.29
Seller-financed transactions (see Deferred payment to seller, above)
Seller of property, state withholding of purchase price, 1.85
Short sales, tax considerations, 6.106F
Terminology for calculating gain, 9.25
Transfer taxes
Generally, 4.134, 6.95
Documentary transfer tax. See **Documentary Transfer Tax**
Williamson Act, tax incentives under, 1.86, 4.93
Withholding taxes
Escrow. See **Escrow**
Real estate salespersons, withholding taxes from compensation of, 2.19
Residential purchase and sale transaction, state and federal withholding taxes, 6.94
State withholding of purchase price, 1.85
Wraparound financing, 9.29, 9.58, 9.60

Tenancy-in-Common
See also **Joint Tenancy**
Generally, 6.88
Adverse possession by tenants in common, requirements for acquisition of title by, 11.77
Agreement, App O
Closing conditions involving multiple sellers, 4.128
Deed, grantee recitals, 10.32
Deferring capital gains through tenancy-in-common transaction to acquire fractional interest in commercial properties, 1.96
Joint tenancy distinguished, 4.22
Partition rights, 4.23

Termination of Transaction
Breach of contract as grounds for, 4.164
Business operations of sale property, 4.84, 4.104
Conditional purchase and sale agreement, 4.3, 4.99-4.100, 4.174
Escrow. See **Escrow**
Joint tenancy, 4.22, 6.87, 10.58
Listing agreements. See **Listing Agreement**
Option, termination of. See **Options**
Partitioning cotenancy, 4.23
Remediation assurances lacking, 7.58, 7.92
Tenant's lease, 4.72, 4.74, 4.103, 4.136, 10.48
Time of essence, 4.152, 4.178
Transfer disclosures made after execution of contract as grounds for termination of offer, 6.35

Termites. See **Pests and Pest Control**

Terrorism
Generally, 13.124
Transactions involving suspected terrorists, prohibitions against engaging in, 1.59, 4.119

Tests and Studies of Property. See **Inspection of Property**

Third Parties
Attorney's duty of care owed to third parties, 9.5
Brokerage transaction. See **Brokers, Dealers, and Real Estate Salespersons**
Consent to joint tenancy between one spouse and another person, 10.40
Contaminated property remediation costs
Agreements limiting remediation costs, effect on third parties, 7.21, 7.61
Buyer's indemnity of seller for third party claims, 7.69
Lender indemnity, 7.90, 7.92, 7.95
Offset against buyer's note, third party establishing amount, 7.83
Remediation liability, third party defense, 7.22-7.23
Covenant for further assurance, seller's action against third party for breach of, 12.16
Deeds
Conveyance on distribution of trust, protection for third parties dealing with trustee, 10.47
Delivery of deed to third party, effect of, 10.72
Description of property, inspection to ascertain third party rights, 11.11
Due diligence, determining consents or waivers from others necessary, 1.10, 1.66-1.67, 1.92
Escrow holder. See **Escrow**
Indemnification (see Contaminated property remediation costs, above)
Letter of intent, effect of third party approvals, 3.22

Partnership statement of authority, effect on third parties, 4.24
Purchase and sale agreement
Approval of third party, agreement conditioned on, 4.47
Buyer's review of third party contracts, 4.76
Enforcement of contract made expressly for third party's benefit, 4.163
Wraparound financing, providing, 9.7, 9.56

Timber Harvest Areas
Local ordinances prohibiting timber harvesting within specified zones, validity of, 1.80

Time
See also **Statutes of Limitations**
Balloon payment of seller financing, 9.11
Client's timing needs, 1.37-1.41
Due diligence environmental reports, 7.54, 7.59
Easements, duration of, 11.71
Escrow
Buyer's separate escrow instructions, time for close of escrow, 4.132
Buyer's supplemental escrow instructions on time for closing of escrow, 15.56
Disbursements, time limitations for, 4.35
Seller's separate escrow instructions, time for close of escrow, 4.132
Seller's supplemental escrow instructions on time for closing of escrow, 15.67
Extension of time. See **Extension of Time**
Foreign Investment in Real Property Tax Act (FIRPTA), buyer's time limit for paying withholding amounts required under, 15.84
Letter of credit, extending or renewing, 7.81
Letters of intent, 3.6, 3.11
Listing agreements. See **Listing Agreement**
Mechanics' liens, 4.69
Options
Constructive notice of existence of option to purchase property, expiration of, 8.18
Extension of option. See **Extension of Time**
Length of time for exercising, 8.16, 8.21
Provision in option contract governing time of essence, 8.75
Rule against perpetuities, effect on exercising option, 8.16
Termination of option, failure to exercise option with allowed time period resulting in, 8.32
Prescriptive easements, termination by nonuse for 5-year period, 11.63
Property insurance
Claim-related documents, time limit for insurer to produce, 13.91
Proof of loss, time limit for filing, 13.88-13.89
Recordation of document, timing of, 15.92
Redemption of property in default for unpaid tax lien, 4.60
Removal of tenants, 4.72, 4.103, 4.136
Rezoning, 4.86
Rule against perpetuities. See **Rule Against Perpetuities**
Survival period for warranties, 4.109
Tax election to not apply installment method of reporting gain, 9.24
Time of essence clauses, 4.152, 4.178, 8.75
Urgency to complete transaction, 1.39-1.41

Title
See also **Ownership and Possession**
Adverse possession. See **Adverse Possession**
After-acquired title. See **Deeds**
Broker's breach of duty of care in failing to advise client to investigate title matters, 2.144
CC&Rs. See **Covenants, Conditions, and Restrictions (CC&Rs)**
Cloud on title
Deed subject to lease with option to purchase as cloud on title, 12.23
Removing cloud on title, recital in deed, 10.43
Seller's representations and warranties of no cloud on title, precautions against, 11.75-11.76
Company. See **Title Company**
Condition of title
Generally, 4.111, 6.79
Preliminary report, contents of, 6.80
Purchaser's due diligence, 4.171
Seller's due diligence, 1.61
Unrecorded interests in property, 6.81
Constructive trust, imposition if title obtained through fraud, mistake, or constructive fraud through violation of fiduciary or confidential relationship, 10.19
Corporations. See **Corporations**
Covenants of title. See **Covenants of Title**
Curing defects caused by ancient or expired interests, 4.52, 11.115
Defective title

Buyer's precautions, 4.111, 4.129, 11.75
Cloud on title (see Cloud on title, above)
Covenant of seisin and good title, 12.6
Incomplete, confusing, or erroneous description in deed, 11.91
Overlapping descriptions, 11.89
Quiet enjoyment and warranty, effect of defective title on covenants of, 12.9
Seller's representations and warranties of no cloud on title, precautions against, 11.76
Description of property
Buyer reviewing legal description of property as part of title review, 6.80
Defective title (see Defective title, above)
Off-record matters (see Record title, matters off-record, below)
Reservation or exception, 11.92
Status of title, 11.10
Dominant tenement, identifying, 11.65
Easements. See **Easements**
Encumbrance, taking title subject to, 4.38
Entity to be formed, 4.20
Escrow. See **Escrow**
Importance of ownership form, 4.21
Insurable interest, legal title not controlling for purposes of having, 13.17-13.21
Insurance. See **Title Insurance and Preliminary Report**
Joint tenancy. See **Joint Tenancy**
Marketability of title
Dividing property in violation of Subdivision Map Act, effect on marketability of title, 4.55
Purchase and sale agreement. See **Purchase and Sale Agreement**
Married persons as buyers, community property presumption, 4.21
Married persons selling property, 4.12, 4.19, 10.56
Off-record matters (see Record title, matters off-record, below)
Partnership property, conveyances, 4.24-4.26, 4.156
Performance. See **Performance**
Preliminary report. See **Title Insurance and Preliminary Report**
Presumptions affecting. See **Presumptions and Inferences**
Property insurance policy not transferring with title on sale of property, 13.24
Quiet title. See **Quiet Title**
Record title, matters off-record
Generally, 11.42
Easements. See **Easements**
Residential purchase and sale transactions
Generally, 6.78
Condition of title (see Condition of title, above)
Vesting of title (see Vesting of title, below)
Risk of loss on buyer when transferring title, 13.8
Single purpose entity (SPE), title to property in form of, 9.3
Slander of title by escrow holder, liability for, 15.22
Tenancy-in-common. See **Tenancy-in-Common**
Trustee signing deed as individual, effect on conveyance of title, 10.19
Vesting of title
Generally, 6.86
Buyer's title review, confirming vesting of title as part of, 6.80
Community property. See **Community or Separate Property**
Joint tenancy. See **Joint Tenancy**
Registered domestic partners, title held by, 6.90-6.91
Tenancy-in-common. See **Tenancy-in-Common**
Tenancy in partnership, 6.92
Warranty of title, 4.111

Title Company
Agent for title insurer, underwritten title company as, 15.15
Buyer's right to designate, 4.57
Defect in title and covenant of seisin and good title, 12.6
Description of property
Generally, 11.2
Symbols versus written descriptions, 11.35
Duties of, 6.2
Escrow. See **Escrow**
Independent escrow companies distinguished from, 15.15
Seller's affidavit providing information for title insurer, 15.40
Toxic contamination, title chain reviews, 7.86

Title Insurance and Preliminary Report
Generally, 9.43
Adverse interests, 4.68

ALTA and CLTA policies distinguished, 1.134, 11.11-11.12
Amount, 4.53
Attorneys
Advising client, 1.133
Postclosing follow-up by attorney, receipt and review of title policy, 1.142
Review of documents by, 1.61, 4.19
Buyer's supplemental escrow instructions on title insurance requirements, 15.53
Contents of preliminary report, 4.54, 6.80
Costs of policy and required lead times, 1.139, 4.56, 4.122, 4.134
Covenants of title, effect of, 12.3
Deed in lieu of foreclosure, 10.41
Deed subject to lease containing option to purchase as cloud on title, 12.23
Defects in title, buyer's precautions against, 4.111, 4.129, 11.75
Description of property
Generally, 11.13
ALTA and CLTA policies distinguished, 11.11-11.12
Boundary dispute, title insurance endorsement to cover possible, 6.7
Overlapping descriptions, 11.89
Preliminary report, 11.10
Review by title insurer, 11.5
Review of title insurance policy, 11.10-11.11
Easements, 4.64
Endorsements
Generally, 6.85
Boundary dispute, title insurance endorsement to cover possible, 6.7
Mechanics' lien endorsements, 4.69
Policy endorsements, review use of, 1.136
Subdivision Map Act compliance endorsement, 4.92, 4.114
Survey endorsement, buyer requesting ALTA policy with, 11.75
Exceptions and indemnities to title policies, negotiations about, 11.13, 11.75
Exceptions, preliminary report showing
Buyer's approval as condition to purchase, 4.57, 4.171
Easements, 4.64
Mechanics' liens, 4.69, 4.172
Tax liens, 4.60-4.62
Extended ALTA coverage, 4.57, 4.134
Fees and costs, 4.56
Financial ability of insurer, considerations of, 1.138
Land survey prerequisite, 4.58
Language considerations, 1.137
Means of protecting against defects in title, 4.53
Nature of preliminary report, 4.55
Negotiating exceptions and indemnities, 11.13, 11.75
Option contracts. See **Options**
Problems, 1.135
Purchase and sale agreement, title insurance
Generally, 4.53, 4.122
Adverse interests, 4.68
Land survey prerequisite, 4.58
Minors conveying property, 4.15
Notice of advisability of purchasing title insurance, 6.66
Obligation to provide, 4.53, 4.122
Spousal instruments prerequisite, 4.19
Subdivision Map Act endorsement, 4.92, 4.114
Residential title insurance policies
Generally, 6.82
Coverage statement, 6.83
Exceptions and exclusions, 6.84
Subordination transactions, 9.80
Toxic contamination, title chain reviews, 7.37, 7.86

Tort Liability
See also **Negligence**
Antideficiency laws, inapplicability to court obligations arising out of underlying transaction, 9.8
Bond indenture trustee's right to sue attorney for negligent document preparation, 9.5
Brokers
Breach of fiduciary duty by broker, tort measure of damages for, 2.157
Salesperson, broker's tort liability for actions of, 2.20
Escrow holder's liability for intentional tortious conduct, 15.22
Personal injury. See **Personal Injury**

Toxic Waste. See **Hazardous Materials and Toxic Waste**

Transportation
See also **Streets, Roads, and Highways**
Hazardous substances, remediation transporters liability, 7.11, 7.14, 7.76

Trees. See **Timber Harvest Areas**

Trespass
Contaminated property, owner's right to bring trespass action based on, 7.20

Trust Deeds. See **Mortgages and Trust Deeds**

Trusts and Trustees
Attorney and client funds, deposited in identifiable trust accounts, 1.12
Bond indenture trustee's right to sue attorney for negligent document preparation, 9.5
Certificate of nonforeign status by trust, 15.82
Charitable corporation joint tenant, 4.22
Constructive trust, imposition if title obtained through fraud, mistake, or constructive fraud through violation of fiduciary or confidential relationship, 10.19
Constructive trust, recovery of secret profits from broker through imposition of, 2.160
Deeds
Conveyance on distribution of trust, protection for third parties dealing with trustee, 10.47
Grantor recitals in deed, 10.19
Signature of trustee on deed, 10.61
Reviewing trust document for restrictions on transfers, 4.19

Unconscionability
Home equity sales contract, penalties for unconscionable acts by equity purchaser, 6.109

Underground Storage Tanks
Disclosure requirements concerning, 6.53

Undertakings. See **Bonds and Undertakings**

Undeveloped Property. See **Developers**

Undue Influence
Purchase and sale agreement rescission grounds, 4.8

Unemployment Insurance
Brokers and real estate salespersons, exclusion from unemployment insurance system, 2.17

Unfair Competition
Property insurance, insured suing for bad faith under Bus & P C §17200, 13.122

Uniform Electronic Transactions Act
Writing or signature, electronic record or signature satisfying legal requirement of, 4.12

Uniform Partnership Act, 4.24

Uniform Settlement Statement. See **Real Estate Settlement Procedures Act (RESPA)**

Uniform Vendor and Purchaser Risk Act
Interpretation of, 13.6
Risk of loss, 4.137-4.138, 13.3, 13.6, 13.13

Unincorporated Associations
Grantor recitals in deed, 10.16

Unruh Civil Rights Act
Attorney General's enforcement of, 6.101
Broker's liability to third parties for housing discrimination under, 2.181
Disabled persons, Unruh Act prohibiting housing discrimination against, 6.100

Usury
Real estate broker's exemption from usury for loans secured by real property, 2.9
Seller financing, 9.6
Third party wraparound financing, 9.7

Utilities
Property insurance, exclusion for loss or damage caused by power failure, 13.87

Public utilities
Dedication of land to public entities and public utilities, 11.77
Easements, 4.64, 11.47, 11.57, 11.62

Valuation of Property
See also **Appraisals and Appraisers; Price**
Appraisals and appraisers. See **Appraisals and Appraisers**
Broker's advice on. See **Brokers, Dealers, and Real Estate Salespersons**
Buyer's right to investigate conditions affecting value of property, 6.74
Covenants of title, damages for reduction in value caused by breach of, 12.18
Disclosure of facts materially affecting value of property, 11.76
Eminent domain actions, effect on value, 11.87
Option contract tying up property at current market value in expectation of increase in property value, 8.50
Replacement cash value, completion of repairs or purchase of substitute property as condition precedent to receiving, 13.103
Seller precontract due-diligence, property value considerations, 1.60
Survey of acreage, 4.58

Variances
Conditional use permits and variances, 4.87

Verification
See also **Acknowledgments**
Acknowledgment distinguished from, 10.68
Prisoner's right to contract, 4.18

Vested Rights
Building permit, rights vested, 4.86, 4.89
Death of joint tenant, vesting title in survivor, 4.19
Tentative maps, effect of vesting, 1.84

Vesting of Title. See **Title**

Vicarious Liability
Broker's liability for salesperson's fraud, misrepresentation, or deceit, 2.15

Void or Voidable Transactions
Automatic termination of purchase and sale agreement, 4.3, 4.99
Contracts having unlawful or several objects, 4.10
Deeds
Generally, 10.76-10.77
Deed in lieu of foreclosure, 10.41
Description omitted or uncertain, void conveyance, 10.35
Grantee not designated with certainty, deed void for uncertainty, 10.41
Description of property
Conveyance void if certainty requirement not met, 11.14
Omitted or uncertain description resulting in void conveyance, 10.35
Violation of Subdivision Map Act, voidable transfer, 11.24
Fee agreement, failure to comply with statute as voidable, 1.19
First duly recorded conveyance, effect on subsequent purchaser or mortgagee, 12.2
Minors transferring or holding property, 4.15
Mistake in formation of contract, 4.8
Signature of attorney-in-fact missing, 10.60
Subdivision Map Act noncompliance, 4.92

Waiver
Antideficiency laws, waiver prohibited, 9.8
Conditions of deposit for escrow, waiver of, 15.29
Cotenant's partition rights, 4.23
Deed in lieu of foreclosure, effect of waiver of redemption right, 10.41
Defective title, 11.75
Escrow. See **Escrow**
Hazardous substances. See **Hazardous Materials and Toxic Waste**
Letters of intent, 3.10, 3.14, 3.24
Natural hazard disclosure, waiver prohibited, 6.47
Options. See **Options**
Property insurance policy, insurer's waiver of consent to assignment of, 13.24
Purchase and sale agreement. See **Purchase and Sale Agreement**
Security, contaminated property, 7.93
Seller's due diligence review, determining if waivers from others necessary, 1.67

Spousal waiver, 4.19, App M
Subordinated lien, 9.94, 9.96-9.97
Time of essence clause, party's waiver of, 4.152

Walls
Party walls, 4.65

War, Acts of. See **Acts of God or War**

Warranties
Generally. See **Representations and Warranties**
Purchase and sale agreement. See **Purchase and Sale Agreement**

Waste
Antideficiency protection, inapplicability to waste on property, 9.8
Nonassuming buyer's liability, 9.48
Preexisting encumbrance on property, buyer's liability for waste, 4.42
Tenant remaining in possession after sale, buyer's cause of action, 4.73
Toxic waste. See **Hazardous Materials and Toxic Waste**

Water and Water Rights
See also **Floods**
Adjoining landowners. See **Adjoining Landowners**
Conveyance of water right as interest in land, 12.13
Description of property
Generally, 11.81, 11.110
Avulsion, 11.86
Effect of water on, 11.111
Formerly navigable waters, 11.85
High and low water mark, 11.82
Islands, 11.84
Navigable waters, 11.81-11.86, 11.110
Thread or middle of lake or stream, 11.83
Easements. See **Easements**
Groundwater contamination, 7.4, 7.30-7.31, 7.37
Navigable waters, 11.81-11.86, 11.110
Surface waters, engineering studies and runoff damages, 4.77

Water Heaters
Compliance statement, 6.58

Wear and Tear Damage
Property insurance exclusion for, 13.86

Weather Conditions
Property insurance exclusion for, 13.86

Web Sites. See **Internet**

Wills
Contaminated property remediation liability, 7.22

Window Security Bars
Disclosure requirements, 1.59, 6.45

Wire Transfers
Escrow deposits, 4.35

Withdrawal of Seller from Sale. See **Brokers, Dealers, and Real Estate Salespersons**

Withholding Taxes. See **Taxes and Tax Assessments**

Witness
Execution of document, witness acknowledgment insufficient to prove, 15.89

Words and Phrases. See **Construction and Interpretation; Definitions**

Workers' Compensation
Salesperson, applicability of workers' compensation to, 2.18

Work Product
Expert's work production, protection of, 1.57

Wraparound Financing. See **Mortgages and Trust Deeds**

Writings
Buyer's assumption of existing loan, 9.48
Cotenancy, 4.13
Legal opinions, 1.121-1.125
Purchase and sale agreement requirements. See **Purchase and Sale Agreement**
Statute of Frauds. See **Statute of Frauds**

Zoning
See also **Land Use**
Generally, 4.86, 4.113
Applicable local laws, review of, 1.77, 1.86
Common law duty to disclose improvements made in violation of zoning regulations, 6.31A
Conditional use permits and variances, 4.87
Description of property, zoning considerations, 11.4
Development agreement between landowner and city or county, preserving existing zoning through, 4.86
Disclosure of zoning ordinance violations, 6.31B
Easements, compliance with zoning, 11.6
Future zoning changes, 4.113
Rent control or condominium conversion ordinances, 4.72
Timber harvesting within specified zones, validity of local ordinances prohibiting, 1.80
Warranty of zoning, 4.86, 4.113

© The Regents of the University of California