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“An agreement for the purchase or sale of real property does not have to be evidenced by a formal contract drawn with technical exactness in order to be binding.”

Enforceable Option Agreements**THIS ISSUE**

In September 2007, we reported on a court of appeal decision holding that an option purchase agreement in a residential lease was unenforceable because it was too uncertain. Recently, however, the California Supreme Court has reversed that decision, finding that even though the option was not perfect, it was nevertheless sufficiently certain to be enforced.¹

BACKGROUND

Mr. Patel leased a condominium from Mr. Liebermensch, with an option to renew. Mr. Liebermensch drafted the option, which also contained language granting an option to purchase the condominium at a specified price. The following is his option language, verbatim:

“We propose to rent our condominium at 7255 Navajo Road, Apt. #370, San Diego, CA 92119 at a monthly rate of \$1,400.00 starting August 7, 2003 for one year ending August 6, 2004; with a security deposit of \$1,200.00, and the following option to buy [with option to renew lease up to August 2005]. [¶] Through the end of the year 2003, the selling price is \$290,000. The selling price increases by 3% through the end of the year 2004 and cancels with expiration of your occupancy. Should the option to buy be exercised, \$1,200.00 shall be refunded to you. [¶] Please indicate your acceptance by signing below and returning to me at the above referenced fax.”

After paying rent for about a year, Patel sent a letter dated July 22, 2004 and a notice of exercise of the option to purchase the property, “on the terms and conditions therein set forth and as stated below” (purchase price of \$298,700). Liebermensch responded by preparing a draft real estate purchase agreement, specifying the following terms. This

¹ *Patel v. Liebermensch* (2008) 08 C.D.O.S. 15391

sale would be “as is,” the buyer would make a 10 percent deposit of the purchase price with a certain escrow company, and an escrow period of 90 to 120 days was specified, if necessary, in order for Liebermensch to accomplish a 1031 tax exchange transaction.

In response, Patel sent his own draft real estate purchase agreement that changed some of those terms as follows. After the “as is” provision, he added, “As well Buyers have option to cancel this offer if not fully satisfied.” In place of the 90 to 120 day escrow period, Patel added this paragraph: “If seller will require more than 30 days to close escrow for 1031 exchange. Then buyers will require to deposit only [\$5,000] and seller will be responsible for all escrow and other expenses after 30 days of opening escrow. Seller will have maximum of 120 days to close the escrow.”

Liebermensch did not accept Patel's draft real estate purchase agreement. Later, Patel signed a copy of the Liebermensch version, but the negotiations stopped. Mr. Patel brought an action for specific performance of the option agreement, alleging that the terms of the option were clear – identifying the property to be sold, the price at which it was to be sold, the term of the option, and the parties to the agreement. Mr. Liebermensch argued that the option language was not certain enough to allow the Court to enforce it, and on that basis argued the option was invalid.

IN BRIEF

As summarized by the Supreme Court: In this action for specific performance of a real estate option contract, the Court of Appeal reversed a judgment for the plaintiff. Over a vigorous dissent, the court held that the contract was too uncertain to enforce because it lacked the essential terms of time and manner of payment. We reverse. It is settled that if a contract for the sale of real property specifies no time of payment, a reasonable time is allowed. The manner of payment is also a term that may be supplied by implication, and was not significantly

uncertain in this case. The Court of Appeal majority erred by failing to enforce a straightforward option contract. It also improperly relied on the parties’ conduct after their dispute arose to conclude that they had failed to reach a binding agreement.

CONTRACT INTERPRETATION BACKGROUND

As the Supreme Court said, “settled principles of contract law govern this case. The equitable remedy of specific performance cannot be granted if the terms of a contract are not certain enough for the court to know what to enforce. However, the law does not favor but leans against the destruction of contracts because of uncertainty; and it will, if feasible, so construe agreements as to carry into effect the reasonable intentions of the parties if they can be ascertained.

An agreement for the purchase or sale of real property does not have to be evidenced by a formal contract drawn with technical exactness in order to be binding. Equity does not require that all the terms and conditions of the proposed agreement be set forth in the contract. The usual and reasonable conditions of such a contract are, in the contemplation of the parties, a part of their agreement. In the absence of express conditions, custom determines incidental matters relating to the opening of an escrow, furnishing deeds, title insurance policies, prorating of taxes, and the like. The material factors to be ascertained from the written contract are the seller, the buyer, the price to be paid, the time and manner of payment, and the property to be transferred, describing it so it may be identified.”

HOW WAS THIS LAW APPLIED IN THIS CASE?

“Here, the Court of Appeal agreed with the Liebermensches that the absence of terms specifying the time and manner of payment made the parties’ contract too uncertain to enforce. It is clear, however, that there was no substantial dispute or uncertainty over the manner of payment by Patel. While the purchase agreement drafted by Liebermensch after Patel exercised his option added a requirement that

Patel make a “good faith” 10 percent deposit with the escrow company, and Patel countered with a deposit proposal of his own, these were merely incidental matters that had no effect on the ultimate payment to be received by the Liebermensches at the close of escrow. It was the length of the escrow period, unspecified in the contract, that was the sticking point. [Other case law], however, makes it plain that the escrow period is not a necessary term in a contract of sale, and that in any event “time of payment” is a contract term determinable by implication as a matter of law.”

MISSING TIME OF PERFORMANCE DOES NOT INVALIDATE THE CONTRACT

The Supreme Court distinguished between those instructions given to the escrow company and the contract itself. It’s an important distinction to keep in mind for interpreting real estate purchase contracts.

As set forth in the opinion, “[t]hus, while parties are obviously free to include escrow specifications in the contract of sale, *they are not necessary terms*. Insofar as the period of escrow effectively determines the time of payment, the provisions of Civil Code section 1657 apply to the interpretation of the contract: “If no time is specified for the performance of an act required to be performed, a reasonable time is allowed. If the act is in its nature capable of being done instantly — as, for example, if it consists in the payment of money only — it must be performed immediately upon the thing to be done being exactly ascertained.” A legion of cases supports the proposition that a reasonable time for payment may be implied in a contract for the sale of real property. Under Civil Code section 1657, the purchase price is deemed payable upon delivery of the deed.

INFERRING CONTRACT PROVISIONS FROM CONDUCT

“The Court of Appeal majority recognized that a reasonable period may be supplied by implication,

but decided that here the parties’ unsuccessful attempts to complete the transaction showed the option agreement did not represent a meeting of the minds on all essential terms. This was error. The parties’ conduct subsequent to the formation of a contract, “including the dispute which arises and the remedy sought,” may be relevant in determining which terms they considered essential. However, few contracts would be enforceable if the existence of subsequent disputes were taken as evidence that an agreement was never reached.

In this case, by signing the option contract the Liebermensches bound themselves to its terms. They could have, but did not, provide for an extended escrow period in the contract. The Liebermensches suggest this was a matter left for future agreement, as in [a different case decided by the Supreme Court]. Not so. In [that case] and similar cases, a provision specifically contemplating future agreement on an essential term was held unenforceable. “ ‘[A] promise may be sufficiently definite when it contains an option given to the promisor or promisee, yet if an essential element is reserved for the future agreement of both parties, the promise can give rise to no legal obligation until such future agreement. Since either party by the terms of the promise may refuse to agree to anything to which the other party will agree, it is impossible for the law to affix any obligation to such a promise.’ ”

CONCLUSION

This is a major policy-setting decision by the Supreme Court regarding what is necessary in a contract to make it enforceable. Missing terms may be implied by later conduct, and even timeframes, such as dates for close of escrow and payment of money, may be supplied by the courts. It is important to recognize the Court’s intention to enforce contracts, rather than find them unenforceable.

NEXT ISSUE

Enforcement of Real Property Deed restrictions.

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