

## **Are Commissions Still Owing From Sales That Did Not Close?**

You may be surprised to learn that in today's tough economic climate, brokers may have walked away from earned commissions and not even realized it, and buyers and sellers may still owe a commission even though a deal didn't close.

### **THE SCENARIO**

The all too common scenario is a broker who procures a buyer, or represents a seller, of real property, completes the purchase and sale agreement, and ensures the commission schedule is properly documented and included in the closing documents. The purchase and sale agreement is signed and all that is left to do is sit back and wait for escrow to close and then collect the commission. Unfortunately, the deal falls victim to the current economic conditions and falls apart. No close of escrow, no payment of commissions.

If this sounds familiar, as a broker you may have walked away from a commission you earned, or as a buyer or seller you may still owe a commission.

### **THE AGREEMENT**

When the brokerage agreement or the purchase and sale agreement states the commission is to be paid upon the close of escrow, many brokers, buyers and sellers interpret this to mean that the close of escrow is a requirement before the broker earns its commission. However, the law recognizes that, unless the agreement specifies otherwise, the commission is earned at the time the buyer enters into the purchase and sale agreement (or in some cases sooner when a willing and able buyer is presented) and thus, must be paid regardless of whether escrow closes. *RC Royal Development and Realty Corp. v. Standard Pacific Corp.* (2009) 177 Cal.App.4<sup>th</sup> 1410.

The same holds true for a cooperating broker that is not in contract directly with a seller or buyer, but rather a third party beneficiary of the listing agreement between seller and seller's broker. *Steve Schmidt & Co. v. Berry* (1986)183 Cal.App.3d 1299, 1312.

### **THE PROBLEM**

The confusion arises in understanding when a commission is "earned" vs. when a commission is "payable," or due to be paid. When the agreement states that the commission will be paid upon the close of escrow, some interpret this to mean that the payment of the commission is conditioned upon escrow actually closing. This interpretation is not necessarily correct, as the close of escrow only indicates the time of payment, and it is not an indicator of whether the commission was earned. The obligation to pay the commission may remain even if escrow does not close.

One must look at the terms of the agreement to determine when the commission was earned. Commonly, agreements state that commission is earned upon the purchase of the property. In this instance, courts have ruled that the purchase (unless specifically defined otherwise in the agreement) is at the point in time when the purchase and sale agreement

is signed, regardless of whether contingencies are removed and the sale is consummated. *Kuhl Corp v. Sullivan* (1993) 13 Cal. App. 4<sup>th</sup> 1589. This is because the potential buyer obtains equitable title to the property. *RC Royal Development and Realty Corp., supra*; *Osborn v. Osborn* (1954) 42 Cal.2d 358. (In the *RC Royal* case, the agreement specifically defined purchase as "any direct or indirect beneficial interest in the property" and the *Osborn* case found that upon execution of the agreement, a purchaser acquires "a conditional equitable title to the property in fee simple.")

Some agreements may even state the commission is earned upon presenting a ready, willing and able buyer. In such an instance, the signing of a purchase and sale agreement is not even required, so long as a ready, willing and able buyer is presented. *Steve Schmidt & Co. v. Berry* (1986) 183 Cal.App.3d 1299.

### **THE SOLUTION**

These case rulings may seem counterintuitive to the intent of the buyer or seller to pay commissions only upon a completed transaction of purchase and sale. However, it does not appear that these rulings will change anytime soon. Accordingly, new agreements should be carefully drafted to ensure the intent of the buyer or seller are clear.

Any prior agreements should be reviewed to determine when commissions are earned and determine whether there might be any remaining commission obligations even though there is no closed escrow.