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TRENDS IN REAL ESTATE AND TITLE INSURANCE

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Be Careful What You **Write**

Recent decisions highlight the importance of precision in contracts and e-mails to avoid trouble in the future.

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WHILE the year 2004 saw many real estate related decisions handed down, three in particular presented important issues for decision concerning the enforcement of real estate contracts. Real estate attorneys should be aware of these decisions and guide themselves accordingly both in the drafting and negotiation of contracts.

In June 2004, the Appellate Division reversed the New York County Supreme Court and upheld a contract provision providing for forfeiture of a 25 percent deposit following purchaser's default.

In *Uzan v. 845 UN Limited Partnership*,[1] the plaintiffs challenged their forfeiture of approximately $8 million in deposits paid on several pre-construction luxury penthouse condominiums in Manhattan. The First Department, Appellate Division held that the defendant's retention of a 25 percent deposit following plaintiffs' default and failure to cure was an enforceable contract provision and did not constitute an unconscionable, illegal or unenforceable penalty.

In reaching its decision, the First Department noted that the contract at issue was heavily negotiated between sophisticated parties with equal bargaining power who were each represented by experienced local counsel, and that absent any evidence of overreaching resulting from a disparity in bargaining power, duress, fraud, illegality or mutual mistake, the contract provision must be upheld.[2]

The facts were as follows. In April of 1999, two Turkish billionaire brothers signed pre-construction contracts to purchase a total of seven condominium units in The Trump World Tower, which was to become the tallest residential tower in the world.[3] Four of these units were luxury penthouses located on the 89th and 90th floors.

The parties were each represented by counsel who spent two months negotiating the contracts for the penthouse units. As part of the negotiations, the plaintiffs succeeded in reducing those units' aggregate purchase price to a total cost of approximately $32 million.[4] The plaintiffs also managed to negotiate many other provisions of the standard purchase agreement, including altering the payment schedule for the 25 percent deposit.

Rather than pay the deposit as proposed in the condominium offering plan, the plaintiffs negotiated for a payment schedule that provided for a 10 percent payment upon contract execution, with an additional 7-1/2 percent down payment 12 months later and a final 7-1/2 percent payment 18 months following the contract date. The total deposit for the four penthouse units was roughly $8 million and this amount was paid by plaintiffs into an escrow account as provided by the contracts.

At no time during the negotiations did the plaintiffs object to the contract provision that provided for the total amount of the deposit to constitute a non-refundable down payment. In addition, both the original and amended condominium offering plan prominently disclosed the sponsor's right to retain the entire down payment following an uncured default by any of the purchasers.

Sept. 11, 2001, the day terrorists destroyed New York City's two tallest buildings, was approximately one month before the anticipated closing for the penthouse apartments. Plaintiffs subsequently became concerned with purchasing the penthouse units and failed to appear at the Oct. 19, 2001 closing.

Their attorney sent the sponsor's attorney a letter citing the plaintiffs' view that they were entitled to rescind their purchase agreements in light of the Sept. 11 terrorist attacks due to their concerns over future terrorist attacks in a "trophy" building that was adjacent to the United Nations.[5] That same day, the sponsor sent plaintiffs default letters notifying them that they had 30 days to cure. On Nov. 19, 2001, after plaintiffs failed to cure their default, the sponsor terminated the four purchase agreements and retained the $8 million down payment.[6]

Plaintiffs subsequently filed suit against the sponsor, seeking a declaratory judgment that the down payment was an "unconscionable, illegal and unenforceable penalty."[7] The sponsor cross-moved for summary judgment, in support of which it provided various documents to evidence the common usage of a 20-25 percent down payment in the pre-construction luxury market. Included was an affidavit from Donald Trump, in which he stated that the 25 percent down payments were sought because of the substantial length of time between contract signing and closing, and because of the associated risks.[8]

After hearing oral argument, the lower court granted the sponsor partial summary judgment, finding that plaintiffs forfeited 10 percent of the purchase price under the prior ruling of the Court of Appeals in *Maxton Builders*[9] (which concerned a 10 percent deposit), but that the remainder of the down payment was subject to a liquidated damages analysis to determine whether the damages bore a reasonable relation to the sponsor's actual or probable loss.

On appeal, the Appellate Division reversed and fully granted the sponsor's summary

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judgment motion. In doing so, the panel relied upon the ruling of the Court of Appeals in *Lawrence v. Miller*[10] and noted that over time courts have consistently upheld the *Lawrence* rule and recognized a distinction between contracts involving real estate deposits and those containing general liquidated damage provisions.

While general liquidated damage provisions have traditionally been subject to judicial oversight to confirm the amount of stipulated damages bears a reasonable proportion to the probable loss, real estate deposits have not been subjected to the same scrutiny.[11] Traditionally, parties seeking to recover real estate deposits have only succeeded where they have demonstrated that they had a lawful excuse for failing to perform or were able to show a disparity of bargaining power between the parties, duress, fraud, illegality or mutual mistake.[12]

The *Lawrence* rule was reaffirmed by the Court of Appeals in *Maxton*, which identified two legal principles flowing from *Lawrence*. First, that a seller was entitled to retain a deposit in a real estate contract, without reference to his actual damages. Second, that one who breaches a contract may not recover the value of his part performance. The Court of Appeals concluded that "(e)xcept in cases where there is a real risk of overreaching, there should be no need for the courts to relieve the parties of the consequences of their contract. If the parties disagree with the rule [of *Lawrence*], the time to say so is at the bargaining table."[13]

In applying the holdings of *Lawrence* and *Maxton*, the Appellate Division indicated that "it is clear that plaintiffs are not entitled to a return of any portion of their down payment."[14] The parties in *Uzan* were sophisticated businesspeople who spent two months negotiating the contracts and the provision at issue was a specifically negotiated provision of the contracts.

Further, the record evidenced that it was customary in the pre-construction luxury condominium market to price the risk of default at 25 percent of the purchase price.

Thus, the court held that the plaintiffs were fully aware of and accepted the 25 percent down payment provision. There was no evidence of a disparity of bargaining power, or of duress, fraud, illegality or mutual mistake by the parties in drafting the down payment provision. If the plaintiffs were dissatisfied with the provision, the "time to have voiced objection was at the bargaining table. Because they chose to accept it, they are committed to its terms."[15]

Impact of 'Uzan:' Speak Now or Forever Hold Your Peace. The impact of the Appellate Division's decision in *Uzan* is clear. In negotiating a contract, it is imperative that attorneys address any client concerns prior to execution of the contract. Failing to do so will usually lead to an inference that a party agreed to certain contractual provisions at the outset. Courts will continue to be hesitant to interfere with the bargain struck between sophisticated parties represented by counsel, particularly in the case of real estate contracts where no liquidated damages analysis is warranted.

Breakup Fee? Denied

Courts' reluctance to interfere with contracts negotiated at arm's length between sophisticated parties is further evidenced in a July 2004 decision of the United States District Court for the Southern District of New York. In *Specialty Malls of Tampa, Inc. v. Riverbank Landscape, Ltd.*,[16] the court ruled that the appellant was not entitled to a $60,000 breakup fee because the contract language concerning payment of the fee was clear and unambiguous and the conditions for payment of the fee were not met.[17]

In May 2000, an involuntary bankruptcy petition was filed against Riverbank, which was later converted to a petition under Chapter 11.[18] A Trustee was appointed to oversee sale of Riverbank's assets, including several parcels of real property. Specialty Malls made an offer to purchase one parcel and executed a contract with the Trustee. The contract provided for a breakup fee of $60,000 to be paid to Specialty Malls in the event the property was sold to a third party making a higher or better offer. Specifically, Paragraph 37 of the contract provided in pertinent part as follows:

> (a) The obligations of the parties under this Agreement are and shall be subject to, and contingent upon, obtaining an order from the United States Bankruptcy Court approving this Agreement and the sale of the premises to Purchaser ...;
>
> …
>
> (c) Purchaser ... acknowledges that obtaining the aforesaid order may be subject to any "higher or better" offers from third parties. In the event that such a third-party offer is made, and Seller, in his sole discretion, deems such offer higher or better than that set forth in this Agreement, or if Seller shall be so directed by the Bankruptcy Court, then Seller may elect to cancel and terminate this Agreement.
>
> (d) In the event that this Agreement shall be terminated by Seller as set forth in the preceding subsection (c), then in recognition of the substantial costs incurred by Purchaser in evaluating the premises, negotiating this Agreement and otherwise devoting its time, attention and resources to this transaction, upon closing of the aforesiad [sic] third-party offer, and receipt of the purchase price for the premises, seller shall within a reasonable time thereafter, if authorized by the Bankruptcy Court, pay to Purchaser the sum of $60,000.[19]

An addendum to the contract was later executed by the parties that permitted the Trustee to cancel the contract at his discretion in the event he was unable to obtain satisfactory financial accommodations from mortgagees of the property within 30 days from the date of the contract. The addendum stated, in pertinent part, as follows:

> In the event that the Agreement shall be terminated by Seller as set forth in this Addendum to Rider, then in recognition of the substantial costs incurred by Purchaser in evaluating the Premises, negotiating this Agreement and otherwise devoting its time, attention and resources to this transaction, upon closing of a sale of the Premises with a third-party, and receipt of the purchase price for the Premises, Seller shall within a reasonable time thereafter, if authorized by the Bankruptcy Court, pay to Purchaser the sum of $60,000.[20]

An auction sale for the property was held on Jan. 25, 2002. At the auction, several higher or better offers than Specialty Malls' were made with the highest offer ultimately accepted by the Trustee. On Feb. 5, 2002, the Bankruptcy Court of the Southern District of New York issued an order approving the sale, authorizing the sale to second highest bidder in the event of a default by the highest bidder, and authorizing payment of the breakup fee to Specialty Malls.[21]

With respect to the breakup fee, Paragraph 26 of the Order specifically stated that the "Trustees are hereby authorized to pay Specialty Malls of Tampa, Inc. the sum of $60,000 as its break-up fee upon the closing of the transactions contemplated by *this Order*."[22]

Shortly thereafter, the highest bidder defaulted and the second highest bidder declined to purchase the property.[23] As a result, the property was not sold pursuant to the Jan. 25 auction. A second auction sale was held on Sept. 18, 2002, where the property was sold to another party and the sale subsequently closed.

On Dec. 3, 2002, Specialty Malls filed a motion seeking an order of the Bankruptcy Court directing the Trustee to pay the breakup fee. The Bankruptcy Court denied the motion and Specialty Malls appealed to the district court, arguing that the Bankruptcy Court erred in denying payment of the breakup fee.

The district court affirmed the Bankruptcy Court's decision and ruled that the conditions for payment of the breakup fee as expressed in the contract were not met.[24] According to the contract, the parties chose to restrict payment of the breakup fee to a specific circumstance, namely, the cancellation of the sale contract by reason of the Trustee's acceptance of a higher or better offer, the closing of that offer, and the Bankruptcy Court's approval of payment of the breakup fee.

In the present case, while the initial contract with Specialty Malls was terminated as a result of several higher or better offers, both the sale to the highest bidder and the next highest bidder failed to close. In addition, the payment of the breakup fee authorized by the Bankruptcy Court in its Feb. 5 order was conditioned "upon closing of the transactions contemplated by this Order."[25]

Since the property was sold pursuant to the second auction held on Sept. 18, 2002, and not the Jan. 25 auction to which the previous Feb. 5 order related, the requisite Bankruptcy Court approval to the breakup fee was not obtained. Thus, Specialty Malls was not contractually entitled to a breakup fee.

In affirming the Bankruptcy Court's

decision, the district court focused on the express contract language and noted that the court's objective in interpreting a contract is to "give effect to the intent of the parties as revealed by the language they chose to use."[26] Paragraph 37 of the sales contract "set forth with clarity" the conditions that must be met before Specialty Malls was entitled to a breakup fee and the parties evidently intended to restrict the payment to those particular conditions.[27]

While the parties had amended the contract to address an additional circumstance where Specialty Malls was entitled to a breakup fee, this amendment was "clear on its face" in dealing with that particular circumstance and did not modify the more restrictive standard for payment of the fee contained in Paragraph 37.[28] Significantly, the court stated that it "must assume that if the parties had bargained for a less restrictive set of conditions, that set of conditions would have been stated in the contract."[29]

The court also denied appellant's alternate claim that it was entitled to recovery based on the doctrine of quantum meruit, since "quantum meruit recovery is not available if there is an enforceable contract governing the subject matter."[30]

Impact of 'Specialty Malls': Be Careful What You Write. The district court's decision in *Specialty Malls* reinforces the long standing principle that in interpreting a contract, the court's role is to "give effect to the intent of the parties as revealed by the language they chose to use."[31]

The parties in Specialty Malls executed a contract addendum providing for an additional circumstance under which a breakup fee could be paid. Since the addendum did not modify the original contract language providing for payment of the fee, the court reasoned that the addendum merely addressed an additional circumstance under which a breakup fee could be paid and the original contract language, containing a more restrictive standard for payment of the fee, remained in effect.

The court's ruling in *Specialty Malls* highlights that in drafting contracts, attorneys must ensure that the written agreement accurately reflects the intention of the parties. Where an agreement is clear and unambiguous on its face, a court will be reluctant to look elsewhere to determine the intent of the parties.

E-Mail Signature Is Enough

In addition to using precise language in drafting a contract, attorneys must also be cognizant of the fact that a typewritten signature of a party who sends an e-mail may satisfy New York's Statute of Frauds.[32]

The Supreme Court of New York, Kings County, ruled in *Rosenfeld v. Zerneck*[33] that while it was possible to make a contract for sale of real property by e-mail, in the present case, no contract was created because the e-mails exchanged between the parties did not express the essential terms of the contract.

In *Rosenfeld*, the plaintiffs offered to purchase the defendants' house and followed up with an e-mail confirming their offer. Subsequently, the parties spoke on the phone, after which one of the defendants followed up with an e-mail confirming the general terms of the offer.

The e-mail included the purchase price, a closing date, a statement that there was to be no financing contingency, a statement concerning the timing of certain home inspections, and a statement that a contract would be drawn up and signed after the purchaser's engineer's report was obtained.[34] The e-mail was then signed with a typewritten signature, "With kind regards, Michael."[35]

In reviewing the case law concerning electronic signatures, the *Rosenfeld* court noted a recent decision of the Court of Appeals in *Parma Tile v. Estate of Short*[36] indicated that automatic imprinting of the sender's name by a fax machine did not constitute a signature for the purposes of the Statute of Frauds because the fax machine was automatically programmed to do so, without regard to the applicability of the Statute of Frauds to a particular document.

The court in *Rosenfeld* distinguished that case by noting that the fax transmission in *Parma* did not comply with the Statute of Frauds because there was never any demonstration of the sender's specific intent to authenticate it and *not* because it was transmitted electronically.[37] Had there been a specific intent to authenticate, an electronic signature would have complied with the Statute of Frauds following the Statute's September 1994 amendment permitting a document to be authenticated with an electronic signature.[38]

In *Rosenfeld*, the court held that the defendant's act of typing his name at the bottom of the e-mail manifested his intention to authenticate his signature for purposes of the Statute of Frauds.[39] However, the court ruled that the e-mail did not constitute a binding contract because it failed to lay out all of the essential terms of the agreement.

The e-mail did not indicate any understanding as to the amount of the contract deposit, and further did not specify how the commercial lease encumbering the premises was to be treated. For this reason, the court held that no contract was created because "the parties did not have a meeting of the minds as to the terms of the sale."[40] As a result, the defendant's summary judgment motion was granted.

Impact of 'Rosenfeld': Be Careful What You Type. As e-mail continues to become a more popular method of communicating, it is important to keep in mind the Supreme Court's ruling in *Rosenfeld* that clearly states that an e-mail signature may be deemed a sufficient signature for purposes of the Statute of Frauds. In negotiating contracts by e-mail, prudence dictates that any e-mails sent between the parties clearly indicate that no contract shall be inferred until an actual written contract has been prepared, approved and executed by the parties.

Conclusion

Each of the recent decisions discussed above highlights the need for attorneys to use precise language in drafting contracts (or writing e-mails) to avoid misunderstandings which can lead to years worth of aggravation and costly litigation for a client. While negotiating a contract it is also imperative to make sure that a client's concerns are adequately addressed since courts have traditionally been reluctant to interfere with an arm's length bargain struck between sophisticated parties represented by counsel.

By exercising caution at the outset, attorneys can obtain better results for clients and successfully manage clients' expectations.

1. *Uzan v. 845 UN Limited Partnership*, 778 N.Y.S.2d 171 (1st Dept. 2004).
2. Id. at 178.
3. Id. at 172.
4. Id. at 173.
5. Id.
6. Id. at 174.
7. Id.
8. Id. at 174-175.
9. Id. at 175 (citing *Maxton Builders, Inc. v. Lo Galbo*, 68 N.Y.2d 373 (1986)).
10. Id. at 175-176 (citing *Lawrence v. Miller*, 86 N.Y. 131 (1881)).
11. Id. at 176.
12. Id. (citing to *Cipriano v. Glen Cove Lodge #1458*, 1 N.Y.3d 53 (2003)) (holding that the buyer was entitled to a return of the down payment after seller materially breached its obligations to the buyer, giving the buyer a lawful excuse not to appear at the closing).
13. Id. at 176.
14. Id. at 178.
15. Id. at 178.
16. *Specialty Malls of Tampa, Inc. v. Riverbank Landscape*, 2004 U.S. Dist. LEXIS 13572.
17. Id. at 10.
18. Id. at 1-2.
19. Id. at 2-3.
20. Id. at 4.
21. Id. at 5.
22. Id. (emphasis added).
23. Id. at 5-6.
24. Id. at 8-9.
25. Id. at 9.
26. Id. at 7-8 (citing to *Seiden Assoc, Inc. v. ANC Holdings, Inc.*, 959 F.2d 425 (2d Cir. 1992)).
27. Id. at 9.
28. Id. at 11.
29. Id.
30. Id. at 13 (citing to *Aniero Concrete Co. v. New York City Const. Auth.*, 308 F. Supp.2d 164 (S.D.N.Y. 2003)).
31. Id. at 8 (citing to *Seiden*, 959 F.2d at 428.)
32. General Obligations Law, §5-701.
33. *Rosenfeld v. Zerneck*, 4 Misc.3d 193 (N.Y.Sup.Ct.Kings Cty. 2004).
34. Id. at 194-195.
35. Id. at 195.
36. *Parma Tile Mosaic & Marble Co., Inc. v. Estate of Short*, 87 N.Y.2d 524 (1996).
37. *Rosenfeld*, at 195.
38. General Obligations Law §5-701(b)(4). See also *Page v. Muze*, 705 N.Y.S.2d 383 (2d Dept. 2000) (holding that an e-mail memo with a typewritten signature does not satisfy the subscription requirement of the former Statute of Frauds provision contained in the Uniform Commercial Code (UCC §8-319, repealed L. 1997)). The Uniform Commercial Code §8-113 Official Comment indicates that it is for this reason that UCC §8-319 was repealed.
39. *Rosenfeld*, at 195-196.
40. Id. at 196.

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