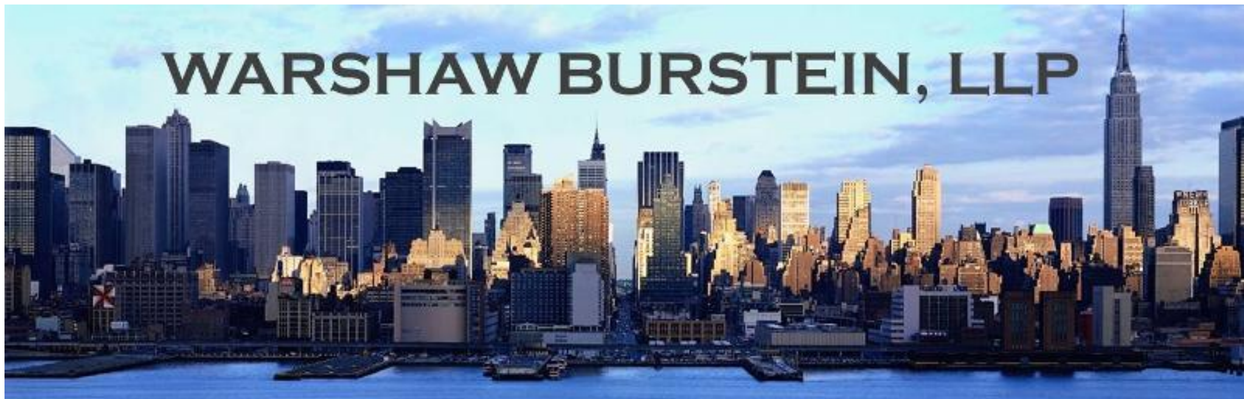

June 3, 2014

CLIENT ALERT

RECOVERING A REAL ESTATE BROKERAGE COMMISSION IN THE ABSENCE OF A WRITTEN AGREEMENT

The importance of having a written agreement, especially in matters involving real estate transactions, cannot be overstated. Recently, in *SPRE Realty, Ltd. v. Dienst*,[1] on an appeal involving a dispute over a real estate brokerage commission, the First Department reminded parties that, in the absence of a written agreement, they will have to abide by a standard to which neither one expressly agreed and that at least one of the parties will not like.

In *SPRE Realty*, defendants, a married couple, retained SPRE, a real estate brokerage firm, in 2006. They reached an "understanding" that the broker would receive a commission after securing a residence that met defendants' expectations. Unfortunately for defendants, such "understanding" was neither reduced to a written agreement nor limited in duration, both of which might have either limited or entirely eliminated their potential liability to pay the broker.

Typically, clients insist upon a provision, in a written brokerage agreement, that the broker's commission shall not be due or earned *unless and until* a closing occurs. This provision protects the clients in that they are liable for a broker's commission only after they have obtained that which they had sought, which, in the case of the defendants in *SPRE Realty*, would have been the purchase of a "luxury residence" in Manhattan. Clients also typically insist upon limiting the duration of a brokerage agreement, usually for a period of six months. This is particularly important for sellers if the broker insists upon an "exclusive" agreement that entitles the broker to receive a commission if the property is sold, even if the sellers find their own buyer.

Brokers, on the other hand, do not want to lose a commission, particularly after all the hard work that they did to bring about the transaction, simply because the parties, for whatever reason, fail to close. Thus, brokers typically insist upon a contract provision that they will be paid a commission merely upon procuring a suitable buyer, irrespective of whether the transaction ultimately closes. Seller's brokers also typically insist upon agreements with the longest possible exclusivity period.

In *SPRE Realty*, according to the facts pleaded in the complaint (which, for the purposes of a motion to dismiss the complaint, must be assumed to be true), the principal and founder of the brokerage firm expended a significant amount of time and effort, over a period spanning 18 months, showing defendants several Manhattan residences. The broker introduced defendants to a new condominium development at 397 West 12th Street. In July 2008, the broker negotiated a deal on behalf of defendants (including obtaining for them a "post-closing discount" in the event of a subsequent sale of a similar unit in the building for less money), and sent a "deal sheet" to the sponsor for the purchase of two units for $11.5 million. Counsel for the sponsor and defendants exchanged and reviewed a proposed contract for the purchase and sale for these two units. The broker also searched for architects capable of executing defendants' specific design plans and introduced them to an internationally-renowned architect, with whom they had a "successful" meeting.

Despite the broker's efforts, about month later, in late August 2008 (just as the real estate market was about to plunge), defendants suddenly pulled out of the deal, stating that they had changed their minds and were no longer in the market for a new home. The broker, however, kept working with the defendants, and particularly in assisting the wife, who was looking for a commercial property for her art and antiques store. In communications with the broker, the wife claimed that she and her husband had no "lingering interest" in the units at 397 West 12th Street.

However, within 18 months of walking away from the purchase of the two apartments, in February 2010 defendants purchased a duplex apartment at the same building, comprised of a different pair of units, and for a much lower price ($6.5 million instead of $11.5 million), evidently taking advantage of the sharp drop in real estate prices that occurred after the 2008 financial crisis. Notably, defendants did not pay a commission to the broker who had brought them to that condominium building in the first instance.

More than three years later, in May 2013, the broker sued defendants, alleging breach of an implied contract and unjust enrichment. Defendants moved to dismiss the complaint, claiming that the broker could not prove that it was the "procuring cause" of the real estate transaction that occurred 18 months later and for different units (albeit in the same building).

The lower court denied defendants' motion to dismiss the complaint, which decision was affirmed by the First Department. In *SPRE Realty*, the First Department held that, in the absence of an agreement to the contrary, the real estate broker will be deemed to have earned the commission when he or she produces a buyer who is "ready, willing and able to purchase at the terms set by the seller."[2] The Court took the opportunity to "clarify" the standard by which a broker may be found to have been the "procuring cause" of a real estate transaction, holding that

there must be a "direct and proximate link" between the introduction of defendant buyers and the seller and the consummation of the transaction.

In adopting this standard, the Court discussed (and rejected) "varying language" used by the First Department itself and other Departments as the standard in prior decisions. One of these was the so-called "amicable atmosphere" standard, where the broker created an amicable atmosphere in which negotiations went forward. The other was the so-called "amicable frame of mind" standard, where the broker brought the parties together in an amicable frame of mind that permitted them to work out the terms of their agreement. The Court found both of these standards to be somewhat "broader and more amorphous" than the requirement of a "direct and proximate link," the standard that it ultimately adopted and which the Court of Appeals previously recognized in a 1980 decision.[3]

The Court found that even under the more exacting "direct and proximate link" standard, the broker's complaint in *SPRE Realty* sufficiently pleaded a cause of action that the broker was the "procuring cause" of the second transaction, even if it was for different units (but in the same building) and the sale occurred 18 months later.[4]

The lesson here is that had defendants insisted upon a written brokerage agreement that expressly set forth the parameters under which the broker would be entitled to be paid a commission, and limited the duration of such agreement, the result might well have been different.

If you have any questions concerning real estate brokerage commissions or any other real estate-related litigation matters, please contact the following attorneys at our firm:

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[1] 2014 NY Slip Op 03642 (1st Dep't) (May 20, 2014).

[2] Id., citing Lane-Real Estate Dep't Store, Inc. v. Lawlet Corp., 28 N.Y.2d 36, 42, 319 N.Y.S.2d 836 (1971).

[3] See Greene v. Hellman, 51 N.Y.2d 197, 206, 433 N.Y.S.2d 75 (1980).

[4] The Court also paved the way for the broker to recover on alternative theories, even if it were ultimately unable to prove that it was the "procuring cause" of the transaction. Thus, the broker would be entitled to a commission if it could show that defendants terminated its activities in "bad faith" and as a mere device to avoid the payment of a commission. In addition, even in the absence of an agreement, the broker could recover in *quantum meruit* for the reasonable value of its services.