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REALTY ADVISORS

## UNDERSTANDING THE PURCHASE AGREEMENT

### WHAT IS IT?

The California Residential Purchase Agreement & Joint Escrow Instructions Form (“RPA”) is the standard legal document used by the California Association of Realtors to outline the terms of most residential transactions. The document provides a customizable framework that fits each transaction. We encourage you to read and understand the entire document but have highlighted some of the more critical components below.

### THE OFFER

A traditional residential real estate transaction begins with a listing broker advertising or ‘listing’ a property for sale. Once listed, a prospective Buyer typically tours the property and decides whether to submit an offer to purchase. The Buyer works with a real estate broker (us) to complete the RPA for submission to the listing broker. It’s important to note that this is merely an OFFER that does not become legally binding until the seller agrees to all proposed terms. Even then, after all terms are initially agreed upon by the Buyer and Seller, the Buyer has **contingency clauses** granting the Buyer the right to unilaterally cancel the contract without penalty within a specified amount of time. These contingencies are in place to protect the Buyer and provide peace of mind when making an offer.

Below are four important RPA terms:

1. **Purchase Price:** The price you offer to purchase the home.
2. **Close of Escrow (COE):** Date you officially own the home. Meaning, the date the grant deed, or other evidence of title transfer, is recorded. This is typically 20-30 days from the date of an accepted offer.
3. **Deposit:** Amount of money deposited with escrow once an offer has been accepted. If the Buyer ends up purchasing the property, the deposit will constitute a portion of the Buyer’s down payment, contribution towards closing costs, or any combination thereof.

This deposit may be refunded to the Buyer under a variety of circumstances so long as the applicable contingency (and corresponding reason for cancellation) remains valid. The deposit is typically 3 percent of the purchase price.

4. **First Loan:** The amount of money borrowed from a financial institution to purchase the home. The down payment dictates the first loan amount. Second or supplemental loans are atypical for residential real estate purchases, so the term ‘first loan’ can be simply viewed as the home loan. The down payment plus the first loan generally equals the home’s purchase price.

**Escrow Defined:** Escrow is a third-party company coordinating with brokers, lenders, buyers, and sellers to manage the sale of the property. It orders reports, collects deposits, transfers title, records legal documents, coordinates loan signing, and helps with a variety of other tasks required to close a transaction. Escrow steps in once the Buyer and Seller have agreed to initial sale terms, thus when a binding contract is created the property is referred to as being “in Escrow”. Lastly, Close of Escrow (COE) is the date or point in time when all transactional items have been completed and title is legally transferred to the new owner.

## CONTINGENCIES

Contingencies are contractual rights given to the Buyer and Seller, which allow for unilateral cancellation of the contract (RPA) - without penalty. Once a contingency has been removed, the removing party may no longer cite that specific contingency as a credible reason for unilateral cancellation. If a party wishes to cancel the contract after contingencies have been removed, he or she has breached the contract and may be subject to penalties. Stated below is the precise language of the Buyer Investigations contingency from the RPA:

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 by either Buyer or Seller must be exercised in good faith and in writing (C.A.R. Form CR or CC).

A. SELLER HAS: 7 (or \_\_\_ ) Days After Acceptance to Deliver to Buyer all Reports, disclosures and information for which Seller is responsible under paragraphs 5, 6, 7, 8B(5), 10A, B, C, and F, 11A and 13A. If, by the time specified, Seller has not Delivered any such item, Buyer after first Delivering to Seller a Notice to Seller to Perform (C.A.R. Form NSP) may cancel this Agreement.

B. (1) BUYER HAS: 17 (or \_\_\_ ) Days After Acceptance, unless otherwise agreed in writing, to: (i) complete all Buyer Investigations; review all disclosures, reports, lease documents to be assumed by Buyer pursuant to paragraph 8B(5), and other applicable information, which Buyer receives from Seller; and approve all matters affecting the Property; and (ii) Deliver to Seller Signed Copies of Statutory and Lead Disclosures and other disclosures Delivered by Seller in accordance with paragraph 10A.

(2) Within the time specified in paragraph 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 (C.A.R. Form RRRR) Buyer's requests.

(3) By the end of the time specified in paragraph 14B(1) (or as otherwise specified in this Agreement), Buyer shall Deliver to Seller a removal of the applicable contingency or cancellation (C.A.R. Form CR or CC) of this Agreement. However, if any report, disclosure or information for which Seller is responsible is not Delivered within the time specified in paragraph 14A, then Buyer has 5 (or \_\_\_ ) Days After Delivery of any such items, or the time specified in paragraph 14B(1), whichever is later, to Deliver to Seller a removal of the applicable contingency or cancellation of this Agreement.

(4) Continuation of Contingency: Even after the end of the time specified in paragraph 14B(1) and before Seller cancels, if at all, pursuant to paragraph 14D, Buyer retains the right, in writing, to either (i) remove remaining contingencies, or (ii) cancel this Agreement based on a remaining contingency. Once Buyer's written removal of all contingencies is Delivered to Seller, Seller may not cancel this Agreement pursuant to paragraph 14D(1).

(5) Access to Property: Buyer shall have access to the Property to conduct inspections and investigations for 17 (or \_\_\_ ) Days After Acceptance, whether or not any part of the Buyer's Investigation Contingency has been waived or removed.

Per the language above, a Buyer has 17 days to complete all Buyer Investigations. However, in current market conditions this is often reduced to 7-10 days. The term “Investigations” is interpreted broadly. This is the period for checking out the neighborhood, conducting a home inspection with a licensed professional, following up with specialized inspections, looking up

crime rates, visiting schools, and conducting any other investigations on all issues affecting the decision to move forward with the purchase of the home. If for any reason during this time, the Buyer realizes the home is not the right fit, the contract may be canceled without penalty.

Within the same 17 days (or fewer), a Buyer may ask the Seller to repair or remedy problems with the home. This action is made on a form called Requests for Repair. Following the home inspection, and all buyer investigations, the Seller may agree to make specific repairs, reduce the purchase price, give the Buyer a credit to reduce closing costs, or any combination thereof to remedy issues uncovered during the investigation period. It's important to note the Seller has no obligation to agree to the Buyer's requests.

### **Appraisal & Loan Contingency**

The two other main contingencies relate to the appraised value of the home and the Buyer's home loan. The specific wording from the RPA is as follows:

**1. APPRAISAL CONTINGENCY AND REMOVAL:** This Agreement is (or  is NOT) contingent upon a written appraisal of the Property by a licensed or certified appraiser at no less than the purchase price. Buyer shall, as specified in paragraph 14B(3), in writing, remove the appraisal contingency or cancel this Agreement within 17 (or ) Days After Acceptance.

**(2) LOAN CONTINGENCY:** Buyer shall act diligently and in good faith to obtain the designated loan(s). Buyer's qualification for the loan(s) specified above is a contingency of this Agreement unless otherwise agreed in writing. If there is no appraisal contingency or the appraisal contingency has been waived or removed, then failure of the Property to appraise at the purchase price does not entitle Buyer to exercise the cancellation right pursuant to the loan contingency if Buyer is otherwise qualified for the specified loan. Buyer's contractual obligations regarding deposit, balance of down payment and closing costs are not contingencies of this Agreement.

The appraisal contingency protects the Buyer from paying more for a property than its current market value. Value is determined by a certified appraiser. The Buyer's lender will order an appraisal from an independent third party to ensure the appraisal is performed fairly without influence from the Seller or Buyer. The loan contingency allows the Buyer to cancel the contract without penalty if the Buyer, in good faith, is unable to secure a loan. This protects the Buyer, for example - if a change in financial standing occurs during the escrow process that hinders the Buyer's ability to secure a loan.

### **Contingency Removal**

Per the RPA, the removal of contingencies is an ACTIVE process. Meaning, that the Buyer must sign a form releasing each specified contingency. Unless otherwise agreed, contingencies remain in place indefinitely until actively removed by the Buyer. To protect the Seller from the Buyer's failure to timely remove contingencies, the Seller may issue the Buyer a **Notice to Perform**. Once delivered, the Buyer typically has two calendar days to remove the specified contingency or the Seller may unilaterally cancel the contract. If a Buyer refuses to release the specified contingency and the Seller unilaterally cancels the contract, the Buyer is entitled to a deposit refund from Escrow.

## Liquidated Damages

To protect the Seller from financial loss if the Buyer breaches the contract, the RPA includes a liquidated damages clause. It should be read in its entirety below:

21. REMEDIES FOR BUYER'S BREACH OF CONTRACT:  
A. Any clause added by the Parties specifying a remedy (such as release or forfeiture of deposit or making a deposit non-refundable) for failure of Buyer to complete the purchase in violation of this Agreement shall be deemed invalid unless the clause independently satisfies the statutory liquidated damages requirements set forth in the Civil Code.  
B. 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. Except as provided in paragraph 14H, release of funds will require mutual, Signed release instructions from both Buyer and Seller, judicial decision or arbitration award. AT THE TIME OF ANY INCREASED DEPOSIT BUYER AND SELLER SHALL SIGN A SEPARATE LIQUIDATED DAMAGES PROVISION INCORPORATING THE INCREASED DEPOSIT AS LIQUIDATED DAMAGES (C.A.R. FORM RID).

Because liquidated damages are limited to the amount of the deposit, the Buyer should carefully choose the amount of money deposited with Escrow. Offers with unusually low deposits may indicate the Buyer is uncommitted. The Seller may be reluctant to accept such offers due to the lack of financial collateral. It is important to consider market conditions and seek advice from a broker when deciding how much to deposit. As a reminder, so long as applicable contingencies remain in place, the Buyer may cancel the contract and receive a full deposit refund without penalty.

## Demand to Close Escrow

Demand to Close Escrow is similar to the Notice to Perform. This form is a demand to the Buyer or the Seller to complete the transaction within three calendar days from delivery. This allows each party the right to enforce the agreed-upon COE date. Market conditions often change, and a delayed COE may result in hardships for both parties. If the time period specified in the demand is not met, the issuing party may unilaterally cancel the contract. If Buyer has removed all applicable contingencies and is unable to complete the transaction within the timeframe specified in the Demand to Close Escrow, the Seller may be entitled to the Buyer's deposit as **liquidated damages**. Below is the precise language:

G. CLOSE OF ESCROW: Before Buyer or Seller may cancel this Agreement for failure of the other Party to close escrow pursuant to this Agreement, Buyer or Seller must first Deliver to the other Party a demand to close escrow (C.A.R. Form DCE). The DCE shall: (i) be signed by the applicable Buyer or Seller; and (ii) give the other Party at least 3 (or \_\_\_\_\_) Days After Delivery to close escrow. A DCE may not be Delivered any earlier than 3 Days Prior to the scheduled close of escrow.

**IMPORTANT NOTE:** Frequently, listing brokers issue a Notice to Perform forcing a Buyer to remove the Loan Contingency. If the Buyer does not remove this contingency within the specified time frame, the Seller has the right to unilaterally cancel the contract. Typically, the Buyer removes this contingency when they are ready to purchase the home, thus preventing the Seller from unilaterally canceling the contract. If the Buyer does not close Escrow within the time specified in the Demand to Close Escrow, the Seller may unilaterally cancel the contract and recover liquidated damages. **As a result, it is critically important to work with a lender that**

***comes highly recommended by your broker. Your lender should be honest, accessible, diligent, and have a track record of closing quickly and on time.***

### **COUNTER OFFERS & ADDENDA**

It is rare for a Seller to outright accept a Buyer's first offer. More commonly, initial offer terms act as a framework for the Seller to issue the Buyer a counteroffer. At which time, the Buyer may agree to the newly proposed terms or counter the Seller's counteroffer. In an instance where there are multiple offers presented to the Seller, a Seller may concurrently issue counter-offers to all parties, each of which may have drastically different terms. There is no limit on the number of counter offers a Buyer or Seller may issue. Typically, in today's environment, it is in a Buyer's best interest to find common ground with the Seller as quickly as possible so the Seller does not have time to leverage other offers against the Buyer. Furthermore, given the contingencies and Buyer protections embedded in the RPA, it is often better to have the exclusive opportunity to purchase the home than to miss out entirely.

Once an offer has been accepted, and Escrow officially opens, the Buyer and Seller may work out future differences through Request for Repairs, or draw up addenda modifying RPA terms. All subsequent modifications to the RPA must be agreed upon in writing by the parties. Since the parties must agree to proposed changes, the Buyer should propose desired changes to the contract prior to the Buyer's removal of contingencies.