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Buyer Beware

Determining Liability When the Deal Falls Apart

By Scott A. Miskimon

Closing is months away and the buyer asks for a *fourth* extension of the closing date. The seller throws up his hands at the buyer's endless delays and indecision, and under a mistaken belief that the third extension of the closing date has expired, faxes a letter demanding a closing *now* or the deal is *off*. Should the buyer's closing attorney step in and try to coax the seller to close? Or should the buyer immediately file suit? And what should the seller's attorney do, particularly if in the meantime the seller agrees to sell the land to someone else?

North Carolina's appellate courts recently decided the case of **Profile Investments No. 25, LLC v. Ammons East Corporation**, 2010 N.C. App. LEXIS 1856, 700 S.E.2d 232 (2010), *disc. rev. denied*, 2011 N.C. LEXIS 247, 707 S.E.2d 240 (2011), and it illustrates the difficulties facing a buyer who believes the seller will not close. Although the plaintiff buyer sued claiming the seller had breached the agreement by reason of a written repudiation and by contracting to sell the property to someone else, the ultimate ruling was that, because of the buyer's conduct, as a matter of law the seller did not breach the contract. The case offers important lessons for counsel representing buyers and sellers, particularly regarding transactions that have been long delayed and where mutual trust no longer exists.

The Deal

In **Profile**, the seller was a North Carolina corporation that owned a seventeen-acre tract of undeveloped land located in southeast Raleigh. The buyer was a single-purpose limited liability company, owned by a Kentucky developer who is also a licensed attorney practicing commercial real estate law. In June 2005, the parties entered into a written purchase and sale agreement. The buyer wanted to develop the land into a strip shopping center anchored by a grocery store. The original closing date was set for December 2005, but the buyer repeatedly requested that the seller grant extensions of time, which it did, and the parties signed three written amendments to the agreement. Consequently, the closing date was extended to July 31, 2007.

The buyer's requests for extensions of the closing deadline were prompted because the buyer wanted more time to market its planned shopping center and line up buyers of outparcels, and most especially, an anchor tenant. In May 2007 – two years after the agreement was first signed – the buyer's broker called the seller and asked for a fourth extension, claiming the buyer needed more time beyond the July 31, 2007 closing date. The seller did not grant this request.

The Seller Seeks a Closing

The seller had long been dealing with a buyer who was unready or indecisive, and who would soon prove inconsistent. Moreover, by mistake the seller believed that June 1, 2007 – rather than July 31, 2007 – was the buyer's deadline to close. In actuality, June 1 was the end of the buyer's due diligence period. Under this mistaken belief as to the closing date, the seller faxed a letter to the buyer's broker to prod the buyer to close. In this letter, the seller's president noted his understanding of the deadline for closing, expressed his frustration about not being able to get a definite date for a closing or confirmation that the seller would in fact close, and stated that "unless you make some other arrangements with me immediately I will consider this Contract null and void on June 1, 2007." The buyer did not respond to this fax and the seller's president sent the letter again one week later indicating that if the deal did not close by June 4, 2007, the seller would consider that the agreement with the buyer would "no longer exist." The parties then spoke and the buyer indicated that the seller was free to sell the property to someone else. Reasonably enough, the seller soon put the land under contract with a second buyer.

The Buyer's Conduct After the Seller's Purported "Repudiation"

The day after that, however, the original buyer reversed course and its broker told the seller that the original buyer would close. Caught by surprise due to the buyer's inconsistency, the seller reasonably reacted to the dilemma of having two buyers by promptly contacting the second buyer and requesting a termination of their contract. A termination was not immediately agreed to, and by mid-June, the deadline for closing with the original buyer was still six weeks away. With the buyer's knowledge, the buyer's closing attorney then sent a letter to the seller stating that "the Buyer is moving forward towards closing on or before July 31, 2007. The Buyer is ready, willing and able to proceed to Closing pursuant to the terms of the Contract." The closing attorney emphasized this point with a sentence that she underlined stating that "the Buyer is ready, willing and able to close the transaction . . . on or before July 31, 2007." The seller's closing attorney responded that the seller was going to write a letter to confirm that the parties' agreement was still in effect and that the seller would close.

The buyer then changed course again and requested that the seller sign a memorandum of contract that would be recorded in order to prevent the seller from selling the land to someone else. The seller

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rejected the document as drafted by the buyer because it did not merely re-state the terms of the purchase and sale agreement, but significantly altered the buyer's duty to close. The seller requested that the memorandum of contract be re-drafted to delete objectionable language. The buyer would not agree to do so. Instead, a few days later the buyer sued for breach of contract and requested specific performance and damages.

At this point the deadline for closing was still five weeks away. A few days after the lawsuit was filed, the seller's president obtained a written agreement with the second buyer to terminate their purchase and sale agreement, which was crucial in allowing the seller to go to closing. The seller's counsel then confirmed for the buyer via email that the seller would close. The buyer's closing attorney replied that she would contact her client and respond with a closing date; she also asked the seller to provide a draft of the deed and other seller documents. The seller complied, sent the draft documents, but also repeatedly asked for a closing date. None was provided. On July 31, 2007 – the deadline for closing – the seller delivered to the buyer's closing attorney an executed deed and other seller closing documents. The same day, the buyer rejected the deed and refused to close. One month later, the buyer amended its complaint as of right and dropped its request for specific performance. Thereafter, the buyer pursued its claim for breach but sought only money damages. The buyer originally estimated its damages at $2.7 million, but later revised its estimate to $6.9 million.

The Twists and Turns in Four Years of Litigation

Litigation over the buyer's claim for damages required extensive discovery and generated a host of motions. A few months after filing suit—and after the buyer and its brokers had been deposed—the buyer moved for summary judgment as to the seller's purported liability for anticipatorily repudiating the agreement. The seller then filed its own motion for partial summary judgment to dismiss the buyer's claim and to have the buyer found liable for breaching the agreement due to the buyer's rejection of the deed that was timely delivered to it. The trial court denied the cross-motions for summary judgment. The seller later moved for summary judgment on the issue of lack of proximate cause, which was also denied. The seller was successful in obtaining an order that compelled the buyer to fully explain its revised damages theory and calculation of $6,900,000. Plaintiff failed to comply with this order, however, and the trial court sanctioned the buyer by excluding the revised damages theory, limiting the buyer to its original $2,700,000 damages theory, and ordering the buyer to pay the seller $11,000 in attorneys' fees. The seller then filed a third motion for partial summary judgment on the grounds that, even assuming that the seller breached, all of the buyer's alleged damages could have been avoided if the buyer had closed when the seller timely delivered a deed to the buyer. This motion was granted, the buyer appealed, and the seller cross-appealed the denial of its first two motions for partial summary judgment.

The Buyer Loses its Lawsuit Because of its Own Conduct

On appeal, the seller won and the buyer lost—but not because of the buyer's failure to mitigate its alleged damages (the third motion for summary judgment). Instead, the North Carolina Court of Appeals ruled that the trial court erred in not granting the seller's first motion for partial summary judgment because, as a matter of law, the buyer had not treated the seller's conduct as a repudiation of the contract.

So what did the buyer do to lose its case? In order to prove anticipatory repudiation, a plaintiff must show an absolute and positive refusal to perform the contract prior to the date on which performance is due. Whether the letter from the seller's president was a repudiation or a mere mistake as to the actual deadline for closing turned out to be a moot point. The Court of Appeals expressly chose not to address that issue. Far more important was the fact that, after receiving the seller's letter, "the undisputed statements and actions of [the buyer] make it clear that [the buyer] did not treat the letter as a repudiation." The Court of Appeals then followed – and extensively quoted – a case from the North Carolina Supreme Court decided nearly a century ago. In particular, the Court of Appeals followed the rule that an anticipatory repudiation "is not a breach of the contract *unless it is treated as such by the adverse party*.' " **Profile**, 700 S.E.2d at 236 (quoting **Edwards v. Proctor**, 173 N.C. 41, 44, 91 S.E. 584, 585 (1917)) (emphasis added).

The Court of Appeals then summarized the reasons why the buyer lost. After receiving the letter that supposedly "repudiated" the contract, the buyer's closing attorney sent the seller a letter demanding that the seller proceed with the contract or be sued. In the buyer's letter, the buyer repeatedly emphasized that it was "ready, willing and able to close" by the stipulated closing date. Although the buyer sued for specific performance of the contract, it continued to inform the seller that it intended to close in accordance with the contract and requested that the seller provide closing documents. Consequently, the buyer's "actions and statements clearly demonstrated that [the buyer] was planning on proceeding with the contract and [it] did nothing to treat [the seller's letter] as a repudiation until [the seller] tendered the deed. Only upon tender of the deed did [the buyer] change its course, and after refusing to accept the deed it had demanded, dropped its claim for specific performance. As [the buyer] did not treat [the seller's] letter as a repudiation, the contract was never breached." **Profile**, 700 S.E.2d at 238.

In light of its ruling, the Court of Appeals remanded the case with orders that the trial court enter a summary judgment in favor of the seller. The buyer further appealed this decision, but the Supreme Court declined to hear the buyer's appeal.

Lessons for a Buyer

Cases like **Profile** involve difficult decisions for buyers and sellers, and their counsel. Where a buyer believes the seller will not or cannot close, but the closing date has not yet arrived, the key initial questions for the buyer are whether the seller has anticipatorily repudiated the

contract, and if so, what proof of repudiation exists. Although anticipatory repudiation need only be proved by a preponderance of the evidence, for a statement or conduct to qualify as a repudiation, it must be a "positive, distinct, unequivocal, and absolute refusal to perform the contract." **Edwards**, 173 N.C. at 44. When an anticipatory repudiation occurs, the plaintiff must choose between two paths: either (1) elect to treat the repudiation as a breach and sue immediately, or (2) elect to ignore the repudiation and proceed with a performance of the contract. A plaintiff cannot do both. *Id*. at 44-45.

Given these choices, and the standard for proving anticipatory repudiation, a buyer faces several challenges and risks. A buyer who claims the seller repudiated and immediately sues the seller runs the risk of being wrong on the issue of repudiation, and putting itself in breach. If the buyer ignores the purported repudiation and instead demands that the seller close, or otherwise acts as if the buyer will perform, the buyer is no longer in a position to claim breach. Consequently, the buyer should not sue prior to the closing date, and must instead proceed with performing its obligations due at closing. If the seller does not deliver a deed at closing, and if the contract does not provide that time is of the essence, then the buyer still cannot claim the seller is in breach. Instead, the buyer must tender payment to the seller's closing attorney to be held in escrow, and give the seller some "reasonable" amount of time to perform. **Fletcher v. Jones**, 314 N.C. 389, 393, 333 S.E.2d 731, 734 (1985). What will constitute a reasonable time will not be known in advance, and will usually only be decided by a jury.

Thus, if a buyer wants to avoid this latter situation, and believes that the seller cannot or will not close, the buyer should either sue immediately after receiving evidence of the anticipatory repudiation or declare in writing that the contract is at an end and that the buyer no longer has any obligation to perform. As to either course of action, however, the buyer should only do so if the seller's repudiation is crystal clear, is in writing, and the buyer and its closing attorney and broker have not taken any action or made any statement to suggest that the buyer is not treating the seller's statement or conduct as anything but a repudiation.

Lessons for a Seller

The seller and its counsel may also face hard choices depending on what actions the seller has taken. If the client has either repudiated the contract or made a statement that might be construed as a repudiation, seller's counsel should determine whether the client is willing to retract the statement and proceed with closing. Because a timely retraction will cut off the buyer's right to immediately sue the seller, the seller's counsel should immediately send a written retraction so that the buyer receives it before any lawsuit is filed. *See* **Nazarro v. Sagun**, 2009 N.C. App. LEXIS 986, at *15-16, 680 S.E.2d 270 (June 16, 2009) (unpublished) (citing RESTATEMENT (SECOND) OF CONTRACTS § 256), *disc. rev. denied*, 2009 N.C. LEXIS 790, 682 S.E.2d 385 (2009). The retraction should include clear and unconditional assurances that the seller intends to timely and properly perform his contract and close per the terms of the agreement. *See* **Homeland Training Ctr., LLC v. Summit Point Automotive Research Center**, 594 F.3d 285, 296 (4th Cir. 2010).

Providing an immediate and unequivocal retraction may not be possible, however, if the seller, under the belief he was free to sell the property to someone else, agreed to sell the land to a second buyer. Independent of any statement from the seller to the original buyer, the act of contracting to sell the property to a second buyer may be deemed to be an anticipatory repudiation of the original contract. *See, e.g.*, **Phoenix Ltd. P'ship of Raleigh v. Simpson**, 201 N.C. App. 493, 505-06, 688 S.E.2d 717, 725 (2009). If the seller finds himself in the position of having contracts to sell the same land to two different buyers, the seller is at risk of being a defendant in two different lawsuits. Therefore, if the client desires to retract his purported repudiation and close with the original buyer, the seller's counsel will first need to negotiate a rescission of the second contract. Without such a rescission, a seller's retraction and assurances of closing under the first contract would not be credible or effective. Thus, the second contract must be nullified in order for the seller to be in a position to close with the original buyer as well as eliminate potential liability to the second buyer. If the seller has doubts that the original buyer will close, the seller should consider entering into a backup contract with the second buyer; this agreement would both rescind the contract with the second buyer and also preserve the relationship, albeit contingent upon the original buyer not closing by a stated deadline.

Conclusion

With the uncertainties facing a buyer and a seller when a deal starts to unravel, the closing attorney for each side has to carefully assess the client's rights and obligations. This analysis cannot be based solely on the language of the contract, but has to take into account the statements and conduct of the client, the other party, and of the brokers and closing attorneys themselves. Further, where an anticipatory repudiation is claimed, litigation could be imminent and may be necessary in order to preserve rights. Consequently, the client may well be best served by having the closing attorney immediately consult with a litigator to analyze the client's situation and develop a strategy that avoids missteps, minimizes risks, and advances the client's objectives. •

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