

Navigating Contingencies in the Contract

In a market where buyers have more leverage, it is more likely that buyers will be able to get an offer accepted with the contractual contingencies remaining intact. Here is what buyers (and sellers) should know about contingencies in the standard Residential Purchase Agreement.

Standard Contract Contingencies

The California Residential Purchase Agreement and Joint Escrow Instructions (C.A.R. Form RPA) includes at least five and as many as seven standard contingencies in the contract. Those contingencies are:

- Loan
- Appraisal
- Investigation of Property
- Review of Seller Documents
- Preliminary (“Title”) Report
- Common Interest Disclosures – If applicable
- Review of Leased or Leaned Items – If applicable

The deadline for removal of each of these contingencies is 17 Days after Acceptance. However, for the contingencies that involve the buyer receiving documents to review, the deadline for removal is 17 Days after Acceptance or 5 Days after Delivery of the relevant documents, whichever is later.

Continuation of Contingency – Active Removal Requirement

It is important to remember that the contingencies in the RPA do not go away automatically. The RPA requires something called active removal of the contingencies. As outlined in Paragraph 14B(4) of the RPA, even after the deadline specified in the contract, the buyer retains the right to cancel based on the good faith exercise of any contingency that has not yet been removed in writing. If the seller wants to enforce the deadline, they may send a Notice to Buyer to Perform, and then cancel the contract if the buyer still does not remove the contingencies.

Good Faith Exercise of Contingencies

Some buyers have the mistaken impression that simply having any contingency in place is a sort of “get out of jail free” card that allows them to cancel and get their deposit back no matter what. Buyers need to remember that contingencies must be exercised in good faith. In other words, the reason the buyer is canceling must actually be tied to whichever contingency they are citing as the basis for their cancellation. Such reasons may include but are not limited to: canceling based on the appraisal contingency if the appraisal comes in low, canceling based on the loan contingency if the buyer ultimately does not qualify for the loan, or canceling based on the investigation contingency if buyer’s inspections reveal defects that the buyer is not comfortable with. Paragraph 8 of the RPA goes into more detail regarding what issues are covered by each of the contractual contingencies.

Deposit Issues

Remember, cancellation is a two-step process. The buyer may unilaterally cancel the *contract* based on the good-faith exercise of a remaining contingency, but canceling *escrow* and having the deposit released to either party will always require mutually signed escrow instructions, or potentially a judicial decision or binding arbitration award. Paragraph 14H of the RPA outlines how deposits will be handled at the time of a cancellation. That paragraph advises the parties that they could be subject to a civil penalty of up to \$1000 if they refuse to sign cancellation instructions when there is no good faith dispute as to who is entitled to the funds. However, it also reminds both buyers and sellers that neither agents nor escrow holders can advise as to what constitutes acting in good faith, and that both buyers and sellers should seek legal advice in the event of any disagreement over the deposit release.