

# Enforceability of Purchase Agreements Remains Uncertain Pending California Supreme Court's Decision

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On September 17, 2008, the California Supreme Court agreed to review the decision of the Third District Court of Appeal in *Steiner v. Thexton*, a controversial case decided early this summer. *Steiner* held a purchase agreement unenforceable due to lack of consideration because, in short, the buyer reserved a right to terminate in its sole and absolute discretion and recover its entire deposit. The decision called into question the enforceability of the overwhelming majority of real property purchase agreements. As a matter of general practice, these agreements include provisions permitting a buyer to terminate in connection with due diligence, entitlement, environmental or other contingencies without forfeiting any funds.

## What *Steiner* Tells Us

To establish consideration to bind a seller in its promise to sell property, the buyer must confer a benefit on the seller or incur a detriment itself at the time of entering the contract. The benefit (and detriment) can be money or a promise, for example, to conduct investigations or pursue entitlements that the seller specifically desires. However, if the buyer can recover all of its money upon termination at its discretion or if it can terminate the contract before performing its obligations intended as consideration, then the "consideration" fails from the outset. Even if the buyer actually takes



actions that confer a benefit on seller, such as entitling the property, consideration fails if at the time of entering the contract the buyer reserved the right to terminate regardless of performance and recover all funds.

## What *Steiner* Doesn't Tell Us

*Steiner* fails to provide certainty on how to make a contract enforceable under most circumstances where a purchaser needs unfettered discretion to determine whether the property has significant problems or whether it will be suitable for the purchaser's intended use. Payment of non-refundable cash upon contracting is the most concrete way to establish consideration. But how much is enough? Can it be applicable to the purchase price if the deal closes? With respect to an obligation purported to constitute consideration, is a recital stating that

the obligation was specifically bargained for as consideration enough? What obligations are sufficient?

## Pending Supreme Court Resolution

Because the California Supreme Court agreed to review the case, *Steiner* is no longer considered final and thus ceases to be the law. The Supreme Court may have granted review because it intends to change the ruling in *Steiner*. However, the Supreme Court may let the decision stand. Even if it reverses the decision, it may not fully reject the logic of *Steiner*. Further, in the year or more required for the Supreme Court to hear arguments and issue a decision, other courts may adopt a similar logic and void contracts that do not address the issues raised in *Steiner*. During this period of uncertainty, purchasers should consult their legal counsel as to how and whether to address the consideration issues raised by *Steiner*. Given the ambiguities of *Steiner*, no strategy is certain, but the absence of a strategy may significantly reduce the ability of a buyer to enforce its contract.

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