



THE KEYS TO THE HOUSE

Unraveling Damages in Real Property Sales

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*Presented by the Bar Association of San Francisco – Real Property Section and Barristers Environment,
Land Use and Real Estate Section*

THE KEYS TO THE HOUSE: UNRAVELING DAMAGES IN REAL PROPERTY SALES (PART 2 OF 2) – REMEDIES

A. SPECIFIC PERFORMANCE

1. What is Specific Performance? Compels performance under the purchase agreement. Can be used not only to compel sale, but also to partition, exchange, assign lease, renew a lease, create an easement, perform environmental cleanup.
2. Grounds for Specific Performance: A buyer/seller may bring an action seeking an order that the seller/buyer perform as required by the purchase agreement only if:
 - i. Money damages are inadequate.
 - ii. The terms of the purchase agreement are certain and enforceable.
 - iii. The buyer/seller has performed or is willing to perform and remains able to perform.
3. Based on the presumption that land is “unique,” awarding damages to an aggrieved buyer is generally assumed to be an inadequate remedy. Civil Code § 3387
 - i. See *Real Estate Analytics, LLC v. Vallas* (2008) 160 Cal.App.4th 463, 472-473 (acknowledging presumption regarding inadequacy of damages in purchase agreement and stating, “courts routinely grant a plaintiff’s request for specific performance”); See also *Remmers v. Ciciliot* (1943) 59 Cal.App.2d 113, 120.
4. Sellers are generally assumed to have an adequate remedy in the form of money damages.
 - i. Where Seller shows breach of contract remedy is inadequate (i.e., Civil Code § 3307) and seeks specific performance, Seller must remain able to perform contract, i.e., remain able to convey the property.
 - a. By selling the property to a third person, the seller terminates the contract and the right to seek specific performance. (*Hollypark Realty Co. v. MacLoane* (1958) 163 Cal.App.2d 549, 552.)
5. Specific performance is the appropriate remedy for performance of environmental clean-up or of a “continuing duty.”
 - i. A public port district was properly ordered to specifically perform a covenant to periodically dredge a harbor channel located appurtenant to the original landowners’ property. The covenant requiring the district to build and maintain the channel enhanced the value of the land retained by the original owners and was a material factor in their decision to transfer to the district that portion of their land on which a Marina was later built. (*Ellison v. Ventura Port Dist.* (1978) 80 Cal.App.3d 574, 579; see also *Union Oil Co. of Calif. v. Greka Energy Corp.* (2008) 165 Cal.App.4th 129, 135 [“Ellison represents the modern view that a party entitled to specific performance of a continuing duty should receive it whenever it is practically feasible.”].)

ii. Specific performance was the appropriate remedy for breach of an oil field clean-up agreement. Oil companies bargain for clean sites to avoid the risk of liability to regulatory agencies and landowners. Moreover, specific performance is the most direct means of remedying a breach and protecting the environment. (*Union Oil Co. of Calif. v. Greka Energy Corp.*, supra, 165 Cal.App.4th at 135-136.)

6. Lis Pendens recommended.

7. Courts may refuse to grant specific performance where enforcement is complicated. (See generally, *Ellison v. Ventura Port Dist.* (1978) 80 Cal.App.3d 574, 580-581, and cases cited therein; *Moklofsky v. Moklofsky* (1947) 79 Cal.App.2d 259, 262-263 [real property purchase contract also called for construction of staircase].)

i. *Compare with Rescission, infra.*

B. RESCISSION

1. What is Rescission? Rescission is extinguishment of contract. Rescission relates back to formation, negates existence of the contract and restores parties to the positions before the contract was entered into.

2. Grounds for Rescission:

i. Civil Code §§ 1688-1693 control.

ii. Mutual Consent to Rescission. Civil Code § 1689 (a); *Estate of Wong* (2012) 207 Cal.App.4th 366, 383.

iii. Unilateral Rescission on the basis of mistake, duress, fraud or undue influence.

a. Mistake of Fact or Law.

1. See *6 Angels, Inc. v. Stuart-Wright Mortg., Inc.* (2001) 85 Cal.App.4th 1279, 1287-1288.

b. Duress or Undue Influence.

1. See *Kloehn v. Prendiville* (1957) 154 Cal.App.2d 156, 161 (Several factors supported Plaintiff's grounds for rescission: (1) adequacy of consideration, only \$5000; (2) Plaintiff was recovering from surgery when signing the deed and agreement; (3) the court found that the parties were in a confidential relationship, finding that although the parties were not related, they had "established a de facto family.")

c. Fraud.

1. See *Village Northridge Homeowners Ass'n v. State Farm Fire & Cas. Co.* (2011) 50 Cal.4th 913, 921 (where consent to contract is induced by fraud, a party seeking to void the contract must rescind.)

iv. Court must effectuate rescission.

a. Difficulty in unwinding “years old” purchase of residential real property and alleged prejudice to sellers are not bases to refuse to effectuate rescission where sellers engaged in clear misrepresentation regarding property's sewer system and buyers satisfied all procedural requirements. (*Wong v. Stoler* (2015) 237 Cal.App.4th 1375, 1388-1389.)

3. Notice Requirement and Waiver

i. Civil Code § 1691(a) requires that notice of rescission be given “promptly” upon discovering facts entitling party to rescission.

a. Service of a complaint seeking rescission “shall be deemed to be” the requisite notice. (Civil Code § 1691; *Wong v. Stoler* (2015) 237 Cal.App.4th 1375, 1385-1386.)

ii. Delay in providing timely notice will amount to a *waiver*, *only if* the delay has *substantially prejudiced* the other party. (Civil Code § 1693; *Williams v. Marshall* (1951) 37 Cal.2d 445, 455.)

a. In *DM Residential Fund II, LLC v. First Tennessee Bank Nat'l Ass'n* (9th Cir. 2015) 813 F.3d 876, 877, the Ninth Circuit found that purchaser's two-year delay in pursuing action against vendor deprived it of equitable remedy. The court found that “[i]nstead of investigating and pursuing its claims, [plaintiff] took actions inconsistent with unwinding the contract, including encumbering the property, building improvements, and attempting to sell it. By taking those actions and waiting two years before suing [defendant], [plaintiff] affirmed the transaction, and its right to rescind it is gone.”

4. Restoration of Benefits Requirement

i. Party must restore “everything of value” received under the contract *or offer to restore the benefits* received “upon condition that the other party do likewise” ... unless the other party “is unable or positively refuses to do so.” (Civil Code § 1691(b); see also *Village Northridge Homeowners Ass'n v. State Farm Fire & Cas. Co.* (2011) 50 Cal.4th 913, 921.)

ii. Service of complaint seeking rescissionary relief “shall be deemed” to be the requisite offer. Civil Code §1691.

iii. Full or “in-kind” restoration of benefits is not a prerequisite.

5. Consequential Damages

i. Includes all out of pocket costs incurred in reliance on the contract.

a. This may include, real estate commissions, escrow fees, title charges, interest on specific sums paid to the other party, the value (or cost) of any improvements made to the property, payments made by a rescinding buyer on a mortgage imposed by the seller, and attorney fees (if authorized by the rescinded contract). (*Sharabianlou v. Karp* (2010) 181 Cal.App.4th 1133, 1146.)

ii. Consequential damages may be offset by property's reasonable rental value while rescinding parties are in possession of it. (*Wong v. Stoler, supra*, 237 Cal.App.4th at 1390.)

6. Court may award Punitive Damages.

C. REFORMATION

1. What is Reformation?

i. Reformation lies when, through the parties' fraud or mistake, or one party's unilateral mistake which the other party at the time knew or suspected, the written contract does not truly express the parties' mutual intent.

ii. Usually used to correct mistakes in instruments to reflect the parties' intent. A reformation action asks the Court to revise the contract to make it consistent with the parties' true intentions.

2. Grounds for Reformation:

i. Common law and statutory right. Civil Code § 3399 - 3402.

ii. Mutual Mistake vs. Unilateral Mistake.

a. Unilateral mistake requires plaintiff to prove that the mistake as known to or suspected by the other party to the contract at the time the contract was entered into. Civil Code § 3399

b. Mutual Mistake, Case Example: *Thrifty Payless, Inc. v. Americana at Brand, LLC* (2013) 218 Cal. App. 4th 1230. Shopping center tenant set forth sufficient particular facts to satisfy the pleading requirements to entitle it to reformation of lease based upon mutual mistake where neither party knew common expense estimates were grossly inaccurate. Landlord's agent represented in that tenant's actual percentage of taxes, insurance, and common area maintenance (CAM) was 2.2 percent, rather than 5.67 percent.

iii. Fraud.

a. Reformation is appropriate remedy where one party fraudulently misrepresents the meaning of the contract. However, reformation is not a remedy for fraudulent inducement.

b. Courts may grant reformation to prevent fraud. In *MacFarlane v. Peters* (1980) 103 Cal.App.3d 627,631-633, court properly exercised equitable power to reform treasurer's deed where purchaser at tax assessment sale acquired small parcel of tract, albeit legally, with intent to prevent use of remainder of tract and thereby force owner of balance of tract to negotiate on his terms.

iv. Applies to written contracts, only. *Shupe v. Nelson* (1967) 254 Cal.App.2d 693, 699-700

3. Courts do not have the power to "rewrite" a contract or create a new contract.

i. *Hess v. Ford Motor Co.* (2002) 27 Cal.4th 516, 524; *Shupe v. Nelson* (1967) 254 Cal.App.2d 693, 700; and see *Jensen v. Quality Loan Service Corp.* (EDCA 2010) 702 F.Supp.2d 1183, 1197 (court of equity may revise written instrument only insofar as revisions conform to parties' "real agreement.")

4. May be used as defense to specific performance or damage action.

D. CANCELLATION

1. What is Cancellation? Allows a party to bring an action to cancel an instrument. Whereas rescission restores the parties to their pre-contract position, cancellation leaves the parties as they are at the time of cancellation.

2. Grounds for Cancellation:

i. Civil Code § 3412 may be used to cancel a document where the instrument is:

a. Executed by a person lacking legal capacity;

b. Procured by fraud or undue influence; or

1. See *Schiavon v. Arnaudo Bros.* (2000) 84 Cal.App.4th 374, 378; *Jones v. Adams Fin'l Services* (1999) 71 Cal.App.4th 831, 836.

c. Otherwise legally invalid.

1. See *Ward v. Sup.Ct. (Beverlywood Homes Ass'n)* (1997) 55 Cal.App.4th 60, 67 (motion to cancel homeowner association's recorded notice of noncompliance with CC&Rs brought pursuant to CC § 3412 on ground it was not recordable document.)

ii. Cancellation may not be used where the invalidity is *apparent on the face of the document*. Civil Code § 3413.

3. Only a Court, not a jury, can order an instrument cancelled.

i. See *Santa Ana Mortg. & Invest. Co. v. Kinslow* (1938) 30 Cal.App.2d 107, 109.

ii. Where the invalid document is severable, the court has discretion to order it cancelled *in part*, allowing the balance to remain in effect. Civil Code § 3414

E. CONSTRUCTIVE TRUST

1. What is a Constructive Trust? An equitable principle that one who wrongfully acquires or retains property holds the property as an involuntary constructive trustee for the owner. Purpose is to prevent unjust enrichment.

2. Grounds for Constructive Trust:

i. Authorized by Civil Code §§ 2223 and 2224.

ii. Requires only 3 conditions stated in Civil Code § 2224: 1) existence of property, 2) right of plaintiff to property, and 3) wrongful acquisition or detention of property.

iii. Fraud often involved in constructive trust cases, but may be obtained where there is accident, mistake or undue influence.

3. Tracing: Plaintiff may be required to trace property if defendant took money and converted it into real property.

4. Lis Pendens: Courts have reached contradictory results on allowing lis pendens in constructive trust tracing cases.

i. See *Coppinger v. Superior Court* (1982) 134 Cal.App.3d 883, 890 (lis pendens allowed) versus *Campbell v. Superior Court* (2005) 918. If the purpose of suit to obtain monetary damages, lis pendens is inappropriate. Consider temporary restraining order and preliminary injunction instead.

F. QUIET TITLE

1. What is Quiet Title? Purpose is to resolve an adverse claim to property. Allows plaintiff to secure judgment in rem, i.e., against both known and unknown persons. Quiet Title is appropriate to establish any kind of legal or equitable rights, title, estate, lien or interest in real property against any adverse claim or cloud on title.

2. Grounds for Quiet Title:

i. Code of Civil Procedure §§ 760.010 - 765-060.

ii. Complaint must be 1) verified, 2) include a legal description and common designation of the property, and 3) the adverse claims to title.

a. See *Jensen v. Quality Loan Service Corp.* (EDCA 2010) 702 F.Supp.2d 1183, 1198 (applying Calif. law) (California statutory quiet title action insufficiently pled where complaint failed to allege plaintiff's title, basis of title and adverse claims to title.)

iii. A lis pendens must be filed. Code of Civil Procedure § 761.010(b)

3. Generally a plaintiff must hold legal title to bring a quiet title action, not just equitable title. However, if a party acquires legal title through fraud, then he or she is a constructive trustee and the equitable title holder may pursue a quiet title action. (*Warren v. Merrill* (2006) 143 Cal.App.4th 96, 113.)

4. Quiet Title may be pursued in connection with other remedies. Code of Civil Procedure § 761.010(a)

5. Cause of action to quiet title may contain both equitable and legal considerations. An action to establish only title is equitable. An action to establish title, and gain possession, is an action at law.

i. For example, an action to determine existence of prescriptive easement is one in law, not equity. *Connolly v. Trabue* (2012) 204 Cal.App.4th 1154, 1167.

ii. Note: Jury trial may be unnecessary if the Court first decides the equitable issues and thus disposes of the legal issues. *Nwosu v. Uba* (2004) 122 Cal.App.4th 1229.

