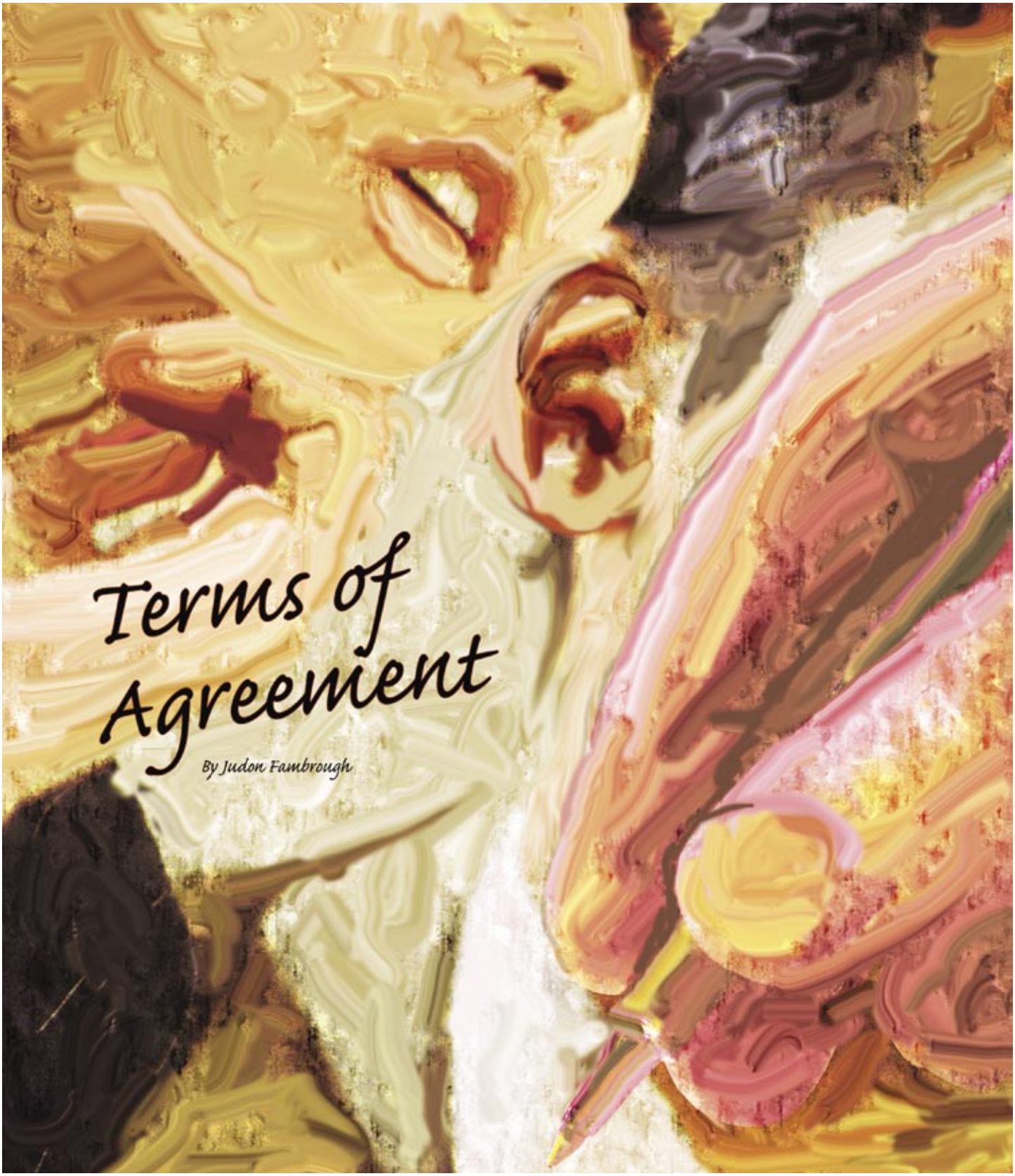
A Reprint from *Tierra Grande*



Two recent Texas appellate court decisions have significant implications for real estate practitioners ranging from brokers and sales agents to inspectors.

Oral Modification of Commission Agreement

As a condition for the receipt of a commission, the Texas Real Estate Licensing Act (TRELA) requires an agreement in writing, signed by the party who agrees to pay the commission. This parallels, in part, the statute of frauds found in the Texas Business and Commerce Code requiring certain contracts to be in writing to be enforceable (Section 26.01).

These rules played a prominent role in determining the outcome of *American Garment Properties Inc. v. CB Richard Ellis-El Paso LLC. (155 SW3rd 431)*. The real estate brokerage firm CB Richard Ellis-El Paso (CBRE) sued American Garments Properties (AGP) to recover a real estate brokerage commission. AGP gave CBRE an exclusive right to sell its property for 12 months. The agreement provided for a 6 percent commission. The listing agreement could be modified but only in writing and if signed by both parties.

Another broker found a buyer, Wal-Mart, for the property. The two brokers agreed to split the commission. At closing, AGP paid the co-broker's commission but not CBRE's. AGP alleged CBRE orally agreed to reduce its commission by $13,500 per month until closing occurred. The broker did not dispute the fact but asserted that any modification to the listing agreement had to be in writing to be enforceable. The trial court agreed and granted CBRE summary judgment.

A trial court grants summary judgment when there is no disagreement about the facts. The judge applies the law to the case by granting a summary judgment to one of the parties. A summary judgment may be appealed, and AGP did.

Among other things, AGP contended that the TRELA requirement applies only to real estate licensees, not to the public. In other words, the broker cannot orally modify the contract and enforce the changes, but the public can.

The appellate court disagreed, ruling that the general principles of contract law, primarily the statute of frauds, apply to everyone. The rule prevents fraudulent oral testimony from altering the terms of a contract. In this case, the contract clearly required any modifications to be written.

However, the court pointed out two exceptions to the statute of frauds. First, it applies only when the oral modification *materially affects* the obligations of the underlying agreement. Second, it does not apply to extensions for the time to perform as long as the oral agreement is entered before the expiration of the written contract. Neither exception applied in this case.

For these reasons, the appellate court upheld the summary judgment but not before asking the Texas Real Estate Commission for a legal opinion. The commission declined but indicated that if the allegations were true, the broker could face disciplinary measures for dishonesty, bad faith and untrustworthiness.

This case sheds no new light on how real estate licensees should conduct business. Instead, it reinforces the old rule that all material changes to a written contract need to be in writing and signed to be enforceable. A handshake does not solidify an enforceable agreement.

Professional Services under DTPA

The case of *Head v. U.S. Inspections Inc.* is the first appellate decision to recognize that some real estate professionals fall under an important exception to the Deceptive Trade Practices Act (DTPA). It also reveals how real estate practitioners may limit their liability (*159 SW3rd 731*).

Head (the plaintiff) contracted with U.S. Inspections (the inspector-defendant) to inspect a dwelling. The contract required that a licensed real estate inspector perform the task but limited the scope to visibly "readily accessible items."

The contract specified that neither the inspection nor the report would include any warranties, express or implied, unless specifically stated. Additionally, the agreement contained a clause limiting liability for "errors and omissions" to the amount paid for the inspection, which could not exceed $500. The limitation-of-liability provision appeared in a display box and was initialed by Head.

An apprentice inspector, not a licensed one, inspected the property. The roof, roof structure and attic were readily accessible and supposedly inspected. The report indicated "evidence of visible water penetration" on the roof but concluded the roof was "performing its function as intended at this time."

Head purchased the property, hired remodeling contractors and met with them on the premises to discuss the alterations. During the meeting, it rained. Water ran down the interior of the kitchen windows and leaked from the living room ceiling. After removing the sheetrock around the kitchen windows, the contractors found water, extensive wood rot, mold and rusty nails. Further inspection revealed water in the light fixtures and water stains on the garage ceiling. Water stains on the living room ceiling had been textured for concealment.

Head sued the inspector for violation of the DTPA, fraud, breach of contract, breach of warranty and negligence. The trial court granted the inspector summary judgment on all but one of the claims. Head appealed.

The appeal focused on two issues, the violation of the DTPA and viability of the limitation-of-liability provision.

The inspector defended the alleged DTPA violations on grounds the services fell under the exemption for professional services of the Texas Business and Commerce Code (Section 17.49[c][1]). The exemption says the DTPA does not apply to rendering professional services, the essence of which is providing advice, judgment, opinion or similar professional

skills. Head countered that the inspector made express misrepresentation of fact "that cannot be characterized as advice, judgment or opinion."

The court disagreed. The contract stated the report would "contain the opinion of the inspector on the need for repair or replacement of the items inspected" and that "It is agreed that the opinions expressed by the inspector are only opinions." Thus, according to the contract, the services rendered were professional opinions exempted under the DTPA. While four exceptions to this rule exist, the court ruled that none applied.

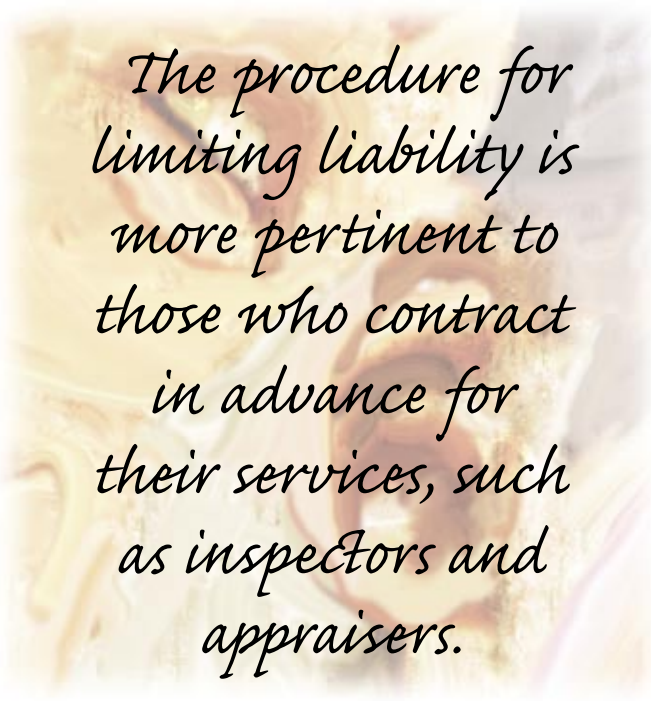
The court found the inspector liable for breach of contract and negligence. However, Head's recovery was limited to $500 because of the limit-of-liability provision. Head appealed, arguing the provision was against public policy and unconscionable.

Public policy, according to the court, depends on the relationship of the parties. If there is no disparity in their bargaining power, public policy is not violated, and the provision is enforceable.

In this case, the court found no disparity. The inspector was not the only provider in the area. Head was free to choose another. Also, a board-certified real estate attorney represented Head throughout the transaction.

As to *unconscionability*, no single test exists to determine if a contract is unconscionable. Generally, the courts address two questions. How did the parties arrive at the terms in controversy (the bargaining process)? Do legitimate commercial reasons justify the inclusion in the contract?

The court did not find the limited liability provision unconscionable. Head was fully aware of the provision during the bargaining process. It was not hidden in the fine print. The provision was conspicuously displayed in a separate box, which Head initialed.



Also, legitimate commercial reasons exist for its inclusion. In the court's opinion, the provision paralleled similar ones addressed in two prior Texas appellate decisions involving an alarm company. In those cases, the courts found it would be unreasonable to expect an alarm company to assume the responsibilities of a burglary insurance policy in exchange for payment of a minimal installation fee. The court viewed home inspectors the same way.

Head paid a small fee for a visual inspection of the dwelling. The task subjected the inspector to significant liability. Without the ability to limit this liability, the costs of home inspection services would likely increase, making them unaffordable for some.

Limitation of Liability Versus Liquidated Damages

The court emphasized the limitation-of-liability provision need not be based on a reasonable estimate of the damages caused by the breach. The reason lies in the difference between a liquidated damages provision and one that limits liability. Both are used to establish the amount of damages before a breach occurs to avoid litigation.

Provisions that fix liability at a specific amount (not the upper limits) or at a specified percentage of the charges for the services are viewed as liquidated damages. To be enforceable, the stipulated amount must be difficult to estimate, yet, at the same time, based on a reasonable forecast. The amount cannot be so large as to be a penalty.

Contractual provisions that set the upper limits of recovery are viewed as limitations on liability. They are not subject to the penalty analysis and need not be based on a reasonable estimate of the resulting damages. However, the provisions must be conspicuously placed in the contract to give fair notice.

Implications for Real Estate Practitioners

The DTPA's professional exemption affects real estate practitioners differently. Clearly, those who give advice and opinions, such as inspectors and appraisers, are more likely covered by the exemption, which provides a strong legal defense, especially when the contract is worded properly as it was here.

Those who primarily represent buyers, sellers, landlords and tenants in real estate transactions must be careful to craft all remarks as advice or opinions. Written verification helps. This is critical when assisting clients in such tasks as setting sales prices or accepting offers, making or accepting counteroffers or helping complete required forms such as property disclosure statements.

The procedure for limiting liability is more pertinent to those who contract in advance for their services, such as inspectors and appraisers. Any limitation should be placed in a separate agreement or conspicuously set apart in the context of the contract. The client should initial or sign the provision in addition to signing the contract. Referencing the fact that other providers of the same services are available in the community may be helpful.

Those who represent buyers and sellers must use contract forms promulgated by the Texas Real Estate Commission with few or no changes. Limiting liability in these situations may be impractical or impossible.

The Head case appears to be one of first impression. Subsequent appellate decisions may follow, overrule, limit, distinguish or expand it. In the meantime, real estate practitioners should not attempt to use one of these techniques to mask shoddy performance or representation. Doing so would violate the canons of ethics.

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